[2010] UKUT 213 (TCC)

Appeal numbers
FTC/04/2009
FTC/05/2009
FTC/28/2009
FTC/32/2009

EUROPEAN LAW – group relief for losses of non-resident subsidiaries – whether there are no possibilities for those losses to be taken into account at the date of the group relief claim – date of valid claim where series of group relief claims – whether valid group relief claim can be made out of time – application of principle of effectiveness – method of quantifying losses for which group relief claim can be made

UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Appellant

- and –

MARKS AND` SPENCER PLC

Respondent

Tribunal: The President, the Hon Mr Justice Warren
Judge Edward Sadler

Sitting in public in London on 1 to 3 March 2010

David Ewart QC and Sarah Ford counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs for the Appellant

Nicola Shaw counsel, instructed by Dorsey & Whitney LLP and Paul Farmer barrister of Dorsey & Whitney (Europe) LLP for the Respondent

DECISION

Introduction

1. This is an appeal from the decisions of the Tax Chamber (Judge Avery Jones and Judge Gammie QC – "**the Tribunal**") of 2 April 2009 (as amended and re-published on 30 April 2009) relating to the availability of group relief for the losses of non-resident subsidiaries ("the **Substantive Decision**") and of 24 August 2009 relating to the quantification of such group relief following the Substantive Decision ("the **Quantification Decision**").

2. The appeal concerns claims by Marks and Spencer plc ("**M&S**") for group relief in respect of the surrender of losses of two subsidiaries, Marks & Spencer (Deutschland) GmbH ("**MSG**") a German company now dissolved and Marks & Spencer (Belgium) NV ("**MSB**") a Belgian company also now dissolved.

3. The Commissioners for Her Majesty's Revenue and Customs ("**HMRC**") appeal against the Substantive Decision on the grounds that the Tribunal did not correctly apply the relevant principles to be derived from the previous cases, and that had the Tribunal done so it would have decided that there were, on the facts, no losses of MSG and MSB in relation to which M&S could properly make a group relief claim. HMRC's case concerns both the time at which M&S is to be treated as having made a valid group relief claim and also whether there were eligible losses at whichever of the dates such a valid claim was properly made. HMRC further argue that, if the Substantive Decision is upheld, so that there are such losses, the Quantification Decision does not correctly determine the method for computing those losses.

4. In summary the issues to be determined in this case are:

   (1) On what occasion or occasions did M&S make a valid group relief claim in relation to the losses of MSG and MSB; and, if it was out of time for making a valid group relief claim, should M&S nevertheless be entitled to make a late claim;

   (2) On the occasion or occasions that M&S made such valid group relief claims did MSG and MSB have losses which, having regard to the tests laid down in the relevant case law, could be claimed by M&S by way of group relief; and

   (3) On the basis that there were such losses which M&S could claim by way of group relief, how should those losses be computed.

5. M&S's claims have resulted in a number of hearings as set out by the Tribunal in paragraphs 1 and 2 of the Substantive Decision. The original decision of the Special Commissioners at the end of December 2002 was appealed to Park J who referred the matter to the European Court of Justice ("**ECJ**"). Following the judgment of the ECJ in December 2005 ("the **ECJ Judgment**"), the matter returned to Park J in 2006, his decision being subject to appeal and cross-appeal to the Court of Appeal. Following the judgment of the Court of Appeal, the matter returned to the first instance tribunal, by then the Tax Chamber, in February 2009. It is from their decision that the HMRC now appeal and M&S cross-appeal.

The facts

6. The facts, which at the hearing before the Tribunal were largely agreed between the parties, are set out in detail at paragraph 5 of the Substantive Decision. A

summary of those facts is sufficient for the purposes of this decision, and is as follows:

(1) M&S is a trading company and a leading retailer in the UK. It is also a holding company for a number of UK and overseas subsidiary companies. It was incorporated and registered in England and Wales and for tax purposes is resident in the UK and is not a dual resident company.

(2) Included in its overseas subsidiaries during the relevant period were MSG and MSB. Although, by reason of various group reorganisations, the corporate structure through which M&S held its interest in MSG and MSB changed from time to time (so that at times some or all of that shareholding was held indirectly through variously another subsidiary and a UK holding company), at all times MSG and MSB were wholly-owned indirect subsidiaries of M&S. Materially, had all the relevant companies, including MSG and MSB, been bodies corporate resident in the UK, they would have formed a group with M&S for the purposes of the group relief provisions.

(3) Neither MSG nor MSB was resident in the UK for tax purposes. MSG was a corporation organised under German law incorporated in November 1995 and resident for tax purposes in Germany only. MSB was a corporation organised under Belgian law and resident for tax purposes in Belgium only. It also operated a branch in Luxembourg which opened in 1998.

(4) MSG was M&S's only subsidiary in Germany. MSG was a trading company operating retail stores and its business commenced in Germany in October 1996. At its height MSG operated seven retail stores in Germany. The statutory accounts of MSG show that it did not make a profit in any year before it ceased trading. It consistently performed below forecasts and expectations, and during its life the M&S group made periodic and significant capital injections and loans to MSG. MSG's trading operations were reduced as from June 1999 and in August 2001 MSG ceased trading following a decision by M&S on 28 March 2001 to divest itself of its entire Continental European activity.

(5) Thereafter MSG generated no further revenue from sales activities and its activities consisted mainly in disposing of its property interests and administering those property interests of which it was unable to divest itself. The disposal of its assets produced cash which was lent within the group producing some interest income, amounting in total to approximately £1.3 million from the year ended 31 March 2002 until liquidation. During that period MSG held a lease of store premises and it sublet those premises to a third party at a small ongoing loss.

(6) On 9 October 2006 (following the ECJ Judgment and Park J's judgment) the shareholder of MSG resolved to appoint a liquidator. The liquidator had resolved matters relating to the store lease and had settled all third party liabilities of MSG by 3 December 2007, and a final distribution of assets in the liquidation took place on 4 December 2007. MSG was dissolved on 14 December 2007, the date on which it was removed from the commercial registry.

(7) MSB operated four retail stores in Belgium and, by way of a branch, a store in Luxembourg. Following the group's decision on 28 March 2001 to withdraw from the Continental European market MSB began to sell its stores. It ceased trading on 22 December 2001. Thereafter MSB generated no further revenue from sales activities and subsequent accounting or tax profits which it made arose mainly from the sale of fixed assets or the reversal of provisions made for anticipated closure costs.

(8) On 30 October 2006 the shareholder of MSB resolved to appoint a liquidator, who was appointed on 31 October 2006. By 23 November 2007 the liquidator had resolved all outstanding debts and claims and had produced a plan for the distribution of assets. On 27 December 2007 MSB was dissolved and the assets of MSB were then held by the liquidator on behalf of MSB's shareholders. On 17 January 2008 the court approved the closure of the liquidation and on 30 January it approved the planned distribution of MSB's assets, which distribution took place on 26 February 2008 and 17 March 2008.

(9) The profits and losses of MSG in its statutory accounts for the periods of account from commencement of its trade until completion of its liquidation, and its profits and losses for German tax purposes for those accounting periods are as follows (all figures in pounds sterling):

Period of Account	Profit/(loss) before tax per German statutory accounts	Profit/(loss) per German tax return
	£	£
31 March 1996	(873,033)	(873,033)
31 March 1997	(6,601,459)	(6,601,459)
31 March 1998	(4,439,205)	(4,439,205)
31 March 1999	(17,506,851)	(17,483,008)
31 March 2000	(30,718,197)	(30,725,152)
31 March 2001	(26,074,802)	(26,082,933)
31 March 2002	7,686,153	2,429,251
31 March 2003	11,550,512	3,826,830
31 March 2004	1,667,086	(1,079,433)
31 March 2005	2,912,981	2,034,322
P/e 8 Oct 2006	217,066	(54,226)
P/e 3 Dec 2007	120,377	(2,410,650)

(10) The profits and losses of MSB in its statutory accounts for relevant periods until completion of its liquidation, and its profits and losses for Belgian tax purposes for those accounting periods are as follows (all figures in pounds sterling):

Period of Account	Profit/(loss) before tax per Belgian statutory accounts	Profit/(loss) per Belgian tax return
	£	£
31 March 1998	(618,388)	(577,988)
31 March 1999	(4,471,511)	(4,445,158)
31 March 2000	(3,045,243)	(3,029,357)
31 March 2001	(42,950,135)	(15,716,115)
31 March 2002	6,608,436	7,879,004
31 March 2003	(1,163,534)	(1,161,968)
31 March 2004	1,004,314	1,004,502
31 March 2005	(54,578)	(54,486)
31 March 2006	(35,494)	(35,236)
31 March 2007	18,133	30,957
P/e 27 Dec 2007	(85,100)	(85,100)

7. It is necessary to deal later in some detail with the various group relief claims which M&S has made in relation to the losses of MSG and MSB, but it is helpful to summarise at this stage the rather complex position, categorising the different group relief claims which were made using the terminology of the Substantive Decision:

(1) In relation to the losses of MSG for each of the individual years 1998 to 2002 (that is, the accounting periods ended on 31 March in those years) M&S made a group relief claim ("**the first group relief claims**"). The first group relief claims were all made before 31 March 2004 (and therefore all before the ECJ Judgment, delivered in December 2005). For the years 1998 and 1999 the first group relief claims were made before MSG ceased to trade, and all of the first group relief claims were made before the liquidator was appointed (October 2006).

(2) In March 2007 (after the Court of Appeal judgment) M&S made further group relief claims in relation to the losses of MSG for each of the years 1998 to 2002 ("**the second group relief claims**"). Each of the second group relief claims was expressed to be in addition to and not in substitution for the corresponding first group relief claim which was not

withdrawn, but M&S undertook to withdraw in due course one or other of the two claims, depending upon which was subsequently allowed.

(3) In December 2007 (after the liquidator had distributed all the assets of MSG but before MSG was dissolved) M&S made further group relief claims in relation to the losses of MSG for each of the years 1998 to 2002 ("**the third group relief claims**"). Each of the third group relief claims was in terms corresponding to the second group relief claims, but taking account of the two extant claims.

(4) The group relief claims in relation to the losses of MSB followed a similar pattern, with the first group relief claims for each of the years 2000 to 2002 made before 31 March 2004, and the second group relief claims for those years made in March 2007 (after the appointment of the liquidator). In June 2007 claims were made, additionally, for losses in the years 1998 and 1999 (these being the first group relief claims for those years). In December 2007 (before MSB was dissolved) the third group relief claims for 2000 to 2002 were made and the second group relief claims for 1998 and 1999 were also made. In June 2008 (following the dissolution of MSB) further group relief claims were made for the losses of MSB for the years 2000 to 2002 ("**the fourth group relief claims**"). These were signed by the liquidator on behalf of the dissolved MSB.

(5) M&S also made group relief claims for losses of MSG for the years 1996 and 1997 and for losses of MSB for the years 1998 and 1999. In the Substantive Decision the Tribunal found that if the losses in those years were utilised on a "first in first out" basis there were no losses for those years which could be claimed by way of group relief. However, if the method of quantifying the losses specified by the Quantification Decision stands there are losses of MSG for 1997 for which it is relevant to determine whether or not the group relief claims made by M&S were valid.

8. A chronology of events and the different group relief claims for MSG and MSB is set out at paragraph 7 of the Substantive Decision, and it is helpful to repeat it here:

	Germany	**Belgium**
31 March 2000	First group relief claim for year 1998	
28 March 2001	Decision to cease trading	
30 March 2001	First group relief claim for year 1999	
August 2001	Ceased trading	
24 September 2001	First group relief claim for years 2000 and 2001	First group relief claim for years 2000 and 2001
22 December 2001		Ceased trading
8 March 2002	Figures for losses adjusted for	Figures for losses adjusted for

	years 1998 – 2001	years 2000 - 2001
17 February 2003	First group relief claim for year 2002	First group relief claim for year 2002
26 March 2004	Amended first group relief claim for year 2002	Amended first group relief claim for year 2002
13 December 2005	ECJ judgment	
10 April 2006	Park J's judgment	
9 October 2006	Resolution to appoint liquidator; published 25-27 October 2006	
30 October 2006		Resolution to liquidate (liquidator appointed 31 October 2006, liquidator approved by court 16 November 2006)
20 February 2007	Court of Appeal judgment	
20 March 2007	Second group relief claims for years 1998-2002; first group relief claim for 1996 and 1997	Second group relief claims for years 2000-2002
27 June 2007		First group relief claims for years 1998 - 1999
3 December 2007	All third-party liabilities paid	
4 December 2007	Distribution of assets	
12 December 2007	Third group relief claims for years 1996-2002	Third group relief claims for years 1998-2002
14 December 2007	Company dissolved	
27 December 2007		Company dissolved and assets held on behalf of the shareholders
17 January 2008		Court approves closure of liquidation
17 January 2008		Court approved distribution of assets which took place on 26 February 2008 and 17 March 2008
31 March 2008		Liquidator signs consent to surrender
11 June 2008		Fourth group relief claim for 2000-2002

9. Although we have referred to the various "claims", there are disputes about whether the purported claims are valid as such quite apart from whether M&S is entitled to any relief in respect of them.

10. In relation to the group relief claims it is important to note that for years up to and including 1999 corporation tax returns and payments were made on what is commonly referred to as a the "pay and file" basis, and that for the year 2000 and subsequent years corporation tax returns and payments have been made on the "self-assessment" basis. Correspondingly, the detailed provisions for making group relief claims differ to reflect the "pay and file" scheme or the "self assessment" scheme, as appropriate. All the group relief claims made in respect of the self assessment years were made within the applicable statutory time limits, but in relation to the pay and file years, where there are more stringent time limits, only the first group relief claims in relation to MSG's losses in those years were made within the applicable statutory time limits.

11. Finally, in summarising the facts, it is necessary to mention that the Tribunal heard expert evidence on the matter of German and Belgian law as to the utilisation of losses for tax purposes in those jurisdictions and also the extent of activities permitted to a company in the course of liquidation. The Tribunal's findings as to German law on the utilisation of losses are found at paragraphs 5(37) – (40) of the Substantive Decision, and as to Belgian law, at paragraphs 5(45) – (48).

12. In formal terms, the original appeal before the Special Commissioners concerned only those appeals which had started with the Special Commissioners in 2002 (and hence those group relief claims which had then been made). The Tribunal had before them, in addition, three joint referrals relating to both subsidiaries in respect of the years ended 31 March 2000, 2001 and 2002.

The group relief legislation – the main provisions

13. Claims for group relief, in a domestic context, are covered by Chapter IV of Part X of ICTA 1988 (sections 402*ff* as amended from time to time). The most important provisions are section 402(1) and section 403(1) which provide so far as material that

> "402(1)….relief for trading losses and other amounts eligible for relief from corporation tax may…be surrendered by a company ("the surrendering company") and, on the making of a claim by another company ("the claimant company) may be allowed to the claimant company by way of a relief from corporation tax called "group relief"….
>
> 403(1) If in an accounting period (the "surrender period") the surrendering company has
>
> (a) trading losses, excess capital allowances or a non-trading deficit on its loan relationships, or
>
> (b) [certain other charges and expenses] which are available for group relief
>
> the amount may, subject to the provisions of this Chapter, be set off for the purposes of corporation tax against the total profits of the claimant company for its corresponding accounting period."

14. As mentioned, the claims in the present case relate to different periods; for accounting periods ending before 1 July 1999, claims fall to be dealt with under the old pay and file regime found in Schedule 17A ICTA 1988 and for accounting periods ending on or after 1 July 1999, claims fall to be dealt with under the current self-assessment regime found in Schedule 18 Finance Act 1998.

Pay and file

15. For pay and file periods, Schedule 17A ICTA 1988 had effect as follows:

16. A company was precluded from making a group relief claim for an accounting period if the company had been assessed to corporation tax for the period and the assessment had become final and conclusive: see paragraph 2. However, this did not apply in the case of a claim made before the end of 2 years from the end of the period. The paragraph applied to the withdrawal of a claim as it applied to the making of a claim.

17. No claim for an accounting period could be made after the end of 6 years from the end of the period except where paragraph 5 applied, that is to say where the company had appealed against an assessment and the assessment had not become final and conclusive. But even where paragraph 5 did apply, the claim still had to be made within 6 years and 3 months: see paragraph 3. HMRC had a discretion to allow a claim to be made after the end of the statutory period. In the present appeal the first group relief claims in respect of losses of MSG in the pay and file years (i.e. for 1998 and 1999) were made within the statutory period, but subsequent claims (including that for 1997 if, as per the Tribunal's Quantification Decision, there are unutilised losses of MSG for that year and the claims made for the losses of MSB for 1998 and 1999) were made outside that period. HMRC have not exercised their discretion to allow late claims.

18. A claim "shall be made by being included in a return under section 11 of the Taxes Management Act 1970 for the period for which the claim is made", and the reference to a claim being included in a return included a claim being included by virtue of an amendment of the return: see paragraph 6. Unless the claim was made pursuant to paragraph 5 (when the precise figure might still have been unknown) the claim had to be for an amount which was quantified at the time it was made: see paragraph 8. A claim under paragraph 5 was required to be expressed to be conditional, as to the amount claimed, on, and only on, the outcome of one or more "relevant matters specified in the claim", that is to say a matter relevant to the determination of the corporation tax assessment of the claimant for the period in question: see paragraph 9.

19. A claim required the consent of the surrendering company. Consent to surrender was of no effect unless the surrendering company gave notice of the consent to its own tax inspector before the claim was made. Nor was it of any effect unless it contained certain specified information including the amount of relief being surrendered: see paragraph 10.

20. All such assessments or adjustments of assessments were to be made as were necessary to give effect to a claim or the withdrawal of a claim.

Self-assessment

21. For self-assessment periods (that is, in the present appeal, for 2000 and subsequent years), Schedule 18 Finance Act 1998 applies. We set out material paragraphs of the Schedule in the Annex to this Decision.

Foreign companies

22. For accounting periods ending on or before 31 March 2000, it was necessary that both the surrendering company and the claimant company should be resident in the United Kingdom, but for later periods group relief could be claimed in circumstances where the surrendering and claimant companies were either resident in the United Kingdom, or non-resident, but carrying on a trade in the United Kingdom through a branch or agency: section 402(3A) and (3B) ICTA 1988.

23. Following the ECJ Judgment, further amendments to the group relief provisions were introduced by the Finance Act 2006. These were intended by the United Kingdom government to give effect to the ECJ's ruling by allowing a United Kingdom resident company to claim group relief for losses of group companies resident in EEA territories. They are to be found in sections 402(2A) and (2B), 403F and Schedule 18A ICTA 1988. They only apply in respect of accounting periods ending on or after 1 April 2006 and do not therefore apply to the losses claimed by M&S in the present appeal.

***M&S* in the ECJ**

24. M&S's case in the ECJ (including the opinion of Advocate-General Poaires Maduro and the judgment of the ECJ) can be found reported as Case C-446/03 *Marks & Spencer plc v Halsey* [2006] Ch 184.

25. The reference to the ECJ related to Articles 43 and 48 EC (which concern freedom of establishment). The ECJ applied a conventional three-stage approach – whether the exclusion from group relief of subsidiaries resident in a different Member State was a restriction on the freedom of establishment; if so, whether such exclusion pursued a legitimate objective compatible with the Treaty; and if so, whether the measures in question went beyond what was reasonably necessary to obtain the objective pursued. The ECJ considered that the fact that UK group relief was not available in respect of losses incurred by a subsidiary resident in another Member State constituted a restriction on the freedom of establishment within the meaning of those Articles. It considered that the restriction on group relief pursued a legitimate objective. But it also considered that, where certain conditions were fulfilled, the measures in question went beyond what was necessary.

26. In reaching the first of those conclusions, the ECJ examined the three factors which had been put forward by the UK and some other Members States to justify the restriction on group relief to losses suffered by resident companies. Those three factors are identified in paragraph 43 of the ECJ Judgment:

> "43. First, in tax matters profits and losses are two sides of the same coin and must be treated symmetrically in the same tax system in order to protect a balanced allocation of the power to impose taxes between the different member states concerned. Secondly, if the losses were taken into consideration in the parent company's member state, they might well be taken into account twice.

Thirdly, and last, if the losses were not taken into account in the member state in which the subsidiary was established, there would be a risk of tax avoidance."

27. The ECJ considered those three factors in paragraphs 44 to 50. We do not need to set out those paragraphs in this Decision. But we do note that nowhere in those paragraphs does the ECJ focus on what concept of "loss" it is adopting in the context of a relief such as group relief. This is perhaps unsurprising since the ECJ remarked, at paragraph 22 that:

> "22. …It is clear from the file before the court that both parties to the main proceedings agree that the losses must be computed on a United Kingdom tax basis. At the tax authority's request, the claimant therefore recomputed the losses on that basis."

28. We will need to return to this aspect when considering the quantification of the loss qualifying for group relief in the present case.

29. The ECJ, at paragraph 51, drew this conclusion:

> "51. In the light of those three justifications, taken together, it must be observed that restrictive provisions such as those at issue in the main proceedings pursue legitimate objectives which are compatible with the Treaty and constitute overriding reasons in the public interest, and that they are apt to ensure the attainment of those objectives."

30. In other words, the ECJ accepted the general proposition that the requirements found in the UK group relief provisions restricting such relief to UK group companies pursued legitimate objectives.

31. The ECJ then went on, in a conventional way, to examine whether or not the restrictions in fact found in the UK legislation went beyond what was necessary to attain those legitimate objectives. As to that, we find in paragraphs 54 to 56 the following:

> "54 The claimant and the commission contended that measures less restrictive than a general exclusion from group relief might be envisaged. By way of example, they referred to the possibility of making relief conditional on the foreign subsidiary's having taken full advantage of the possibilities available in its member state of residence of having the losses taken into account. They also referred to the possibility that group relief might be made conditional on the subsequent profits of the non-resident subsidiary being incorporated in the taxable profits of the company which benefited from group relief up to an amount equal to the losses previously set off.
>
> 55 In that regard, the court considers that the restrictive measure at issue in the main proceedings goes beyond what is necessary to attain the essential part of the objectives pursued where (i) 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 (ii) 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.

56 Where, in one member state, the resident parent company demonstrates to the tax authorities that those conditions are fulfilled, it is contrary to articles 43 EC and 48 EC to preclude the possibility for the parent company to deduct from its taxable profits in that member state the losses incurred by its non-resident subsidiary."

32. The answer to the question was provided in paragraph 59:

"59 Accordingly, the answer to the first question must be that, as Community law now stands, articles 43 EC and 48 EC do not preclude provisions of a member state which generally prevent a resident parent company from deducting from its taxable profits 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 accounting period concerned by the claim for relief and also 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."

33. We refer to the test articulated in paragraphs 55 and 59 as the "no possibilities test". Park J paraphrased the no possibilities test in this way when the case came back to him:

"[31] … [MSG] must have exhausted the possibilities available to it in Germany of having the losses taken into account for the accounting periods concerned by the claim for relief and also for previous accounting periods, if necessary by transferring them to a third party or by offsetting them against the profits made by 'the subsidiary' (presumably [MSG] itself) in previous accounting periods; further … there must be no possibility of [MSG's] losses to be taken into account in Germany for future periods either by [MSG] itself or by a third party, in particular where [MSG] has been sold to the third party. *Mutatis mutandis* the same applies to the losses of [MSB]."

34. The no possibilities test, it can be seen, has two limbs. One limb looks back and one limb looks forward. Under the second limb, it is a question of identifying ways in which the loss might be used and then to assess whether that method of using the loss is a "possibility". Various tests have been suggested for deciding whether a theoretical use of a loss is sufficiently real, or not simply fanciful, as to qualify as a possibility. We will return to the correct test to apply. The decision of the Court of Justice in *M&S* has been referred to in subsequent cases before the ECJ. The first is Case C-374/01 *Test Claimants in Class IV of the ACT Group Litigation* [2006] ECR 1-11673 where Advocate General Geelhoed made some comments directed to it. One senses, perhaps, some unease on his part about the decision in *M&S*. His view was that the obligation to permit set off of the losses of a non-resident subsidiary applied only in "exceptional cases" and the caveat (the no possibilities test) should be applied "extremely restrictively". We do not set out the concerns which led him to express the views. They can be found at

paragraph 65 of his Opinion. They are views no doubt highly influenced by his own perceptions of the potential for distortion of the exercise for the freedom of establishment within the Community which the no possibilities test might have introduced. We do not think that his views can be taken as authority for the proposition that the ECJ Judgment should be applied in a stricter manner than its terms on their face suggest, or that in any way the ECJ Judgment is "special", that is to say, particularly restrictive. The ECJ Judgment has been cited in subsequent cases (see, for example, Case C-311/08 *SGI v Belgian State*, Judgment of 21 January 2010, §56; Case C-196/04 *Cadbury Schweppes* [2006] ECR I-7995, §478; Case C-524/04 *Test Claimants in the Thin Cap Group Litigation v Commissioners of Inland Revenue* [2007] ECR I-2107, §64) without any suggestion that it is to be read or applied in a particularly restrictive way. It is in any event for the national court to apply the ECJ Judgment, and in that regard we have the detailed guidance supplied by Park J and the Court of Appeal.

35. The ECJ applied the criteria set out in paragraphs 55 and 56 of the ECJ Judgment and gave further guidance on the no possibilities test in Case C-414/06 *Lidl Belgium GmbH & Co KG v Finanzamt Heilbronn*, a case relating to losses in the Luxembourg permanent establishment of a German limited partnership. We do not think that the decision adds anything to the principles set out in *M&S* itself.

***M&S*: the return to Park J**

36. M&S's appeal resumed again before Park J, who handed down a judgment on 10 April 2006: *Marks & Spencer plc v Halsey* [2006] EWHC 811; [2006] 3 CMLR 8. In rejecting M&S's submission that the restrictions on group relief provisions in their entirety were unenforceable he said this (a passage quoted by Chadwick LJ when the case found its way to the Court of Appeal which gave its decision on 20 February 2007: see [2007] EWCA Civ 117 [2007] 2 CMLR 21):

> " Legislation of a Member State which imposes a blanket prohibition on intra-Community cross border surrenders of losses is not contrary to Community law, but, on a case by case basis, may not be applied to any case the facts of which correspond to the circumstances described in paragraph 55 of the ECJ judgment."

37. Park J gave some guidance about what the ECJ meant by the "possibilities available". The Tribunal set out a long passage of his judgment from paragraphs 31 to 41. Large parts of these same paragraphs were set out in the judgment of Chadwick LJ when the case reached the Court of Appeal. We do not propose to set out all of these lengthy passages again: they can be easily found but it is necessary to refer to substantial parts of them as they illustrate the approach which the Court of Appeal has endorsed about the correct interpretation of the no possibilities test. We do so by quoting from the judgment of Chadwick LJ, himself quoting extensively from Park J.

38. Starting at paragraph 15 of his judgment, Chadwick LJ said this:

> "15. The Judge set himself the task of explaining 'what the ECJ had in mind by the concepts which it set out in paragraph 55'. He recognised that 'an interpretation may give rise to a question of how it would apply to the particular facts of M&SG or M&SB'. That, he said 'would be a matter to be determined in the first instance by the Special Commissioners'. Nevertheless, there were a number of points to be made. Those follow at [33] to [41] of the judgment.

16. First, as the judge held, " when the ECJ refers to ' possibilities available' it means recognised possibilities legally available given the objective facts of the company's situation at the relevant time". That required consideration of "what is the relevant time"; a question which, as the judge recognised, could be "of considerable importance". Before turning to that question, the judge addressed three other elements: " possibilities legally available, the objective facts of the company's situation at the relevant time, and the possibilities being recognised possibilities". He said this:

> " [34] I start with the assumption, which is certainly correct, that the tax laws of Germany and Belgium do contain provisions under which relief for losses can be obtained in some circumstances. That, however, is not enough to mean that [MSG] and [MSB] could never satisfy the conditions of paragraph 55 of the ECJ judgment. In any developed tax system there will be detailed rules regulating at least the following matters: (1) what kinds of losses qualify for some form of tax relief; (2) for what form or forms of tax relief they qualify; that is what the kinds of profits or income are which, apart from the losses, would be taxable, but against which relief for the losses can be obtained; (3) what the periods are against the profits or income of which the losses can be relieved. These can be complicated matters."

17. At paragraphs [35] and [36] of his judgment Park J illustrated " the range of potential complications" by reference to the availability of tax relief treatment for losses under the domestic law of the United Kingdom; although, as he said

> " the UK rules about the availability of tax relief for losses made by companies are not directly relevant to the present case: it is the German and Belgian rules which are relevant" .

He went on to say this:

> " [37] I have no knowledge of how the detailed rules of German and Belgian tax law operate in relation to these matters, but the application of the criteria in paragraph 55 of the ECJ's judgment requires an ascertainment of what forms of loss relief are provided for in Germany and Belgium and an application of them to the particular circumstances of [MSG] and [MSB]. I do, however, say that in my view the particular circumstances of [MSG] and [MSB] do not for these purposes include the degree of probability or improbability of them returning to profitability in future. Suppose (1) that at the relevant time (which I am going to expand on below) they were still trading; (2) that, if they returned to profit in future accounting periods, their losses would, under German and Belgian tax law, have been relievable against the future profits; but (3) that evidence is given on behalf of M&S that there was little or no real likelihood of their returning to profit in the future. In that case the criteria of paragraph 55 of the judgment would not be satisfied: the objective facts were that the company was still trading and the national tax law permitted past trading losses to be set against future trading profits. With reference to the second of the two indents in paragraph 55 [the second limb of the no possibilities test] it would not be the case that there was no possibility for the losses to be taken into account in Germany and Belgium for future periods: the possibility

> would exist, even if it was unlikely that it would ever happen.[38] I will give one other example to illustrate the same point. Suppose that: (1) one of the companies, say [MSG], had already ceased to trade at the relevant time; (2) German tax law, unlike UK tax law, contained provisions under which [MSG's] unrelieved trading losses from its discontinued trade could be carried forward and used against future income or gains from sources other than the trade (like interest on loans); but (3) the evidence is that the M&S group in general, and [MSG] in particular, had no intention that the company should ever be in receipt of other income or gains in the future. In that situation also the criteria of article 55 would not be satisfied.
>
> [39] Here I give an example which, if it corresponds to the facts of either [MSG's] or [MSB's] losses, would lead to the opposite conclusion. Suppose that the principles of German or Belgian tax law were in all essential respects the same as those of UK law which I illustrated in paragraph 36 above, and that the facts of [MSG] or [MSB] corresponded to those in that illustration. That is, suppose that at the relevant time either company had ceased to trade, that the German or Belgian law did not permit any carry forward of unrelieved losses of a discontinued trade, that all possibilities for which the German or Belgian law provided of carrying the losses back or setting them against other current income had been used, and that there was still a balance of unused losses. Those losses would in my judgment comply with the paragraph 55 conditions, and M&S would in principle be entitled to group relief in respect of them."

18. The judge explained that, in pointing out (at [33] of his judgment) that "possibilities available" meant recognised possibilities, he had included the word " recognised" against the background

> " that the ECJ's formulation effectively places on the claimant for group relief (in this case M&S) the burden of proving a negative: that there were no possibilities of obtaining German or Belgian tax relief for the losses".

He observed that:

> " To prove a negative is always difficult: the litigant is exposed to the risk of it being said that he has identified a number of possibilities and shown that they do not apply in his case, but who can say that there may not be other possibilities which have not been considered at all?".

And he went on:

> "[41] However, a principle which runs through the whole of Community law and has been enunciated by the ECJ in numerous cases

> is the principle of effectiveness: procedures in Member States must not render practically impossible or excessively difficult the exercise of rights conferred by Community law. In my view the burden cast on M&S does require it to ‘ demonstrate’ (the word used in paragraph 56 of the ECJ judgment) that none of the generally recognised means of obtaining tax relief in Germany or Belgium for a company's trading losses existed as possibilities at the relevant time. It does not require M&S to demonstrate more than that. In particular I do not think that M&S should be at risk of losing the case by reason of an argument that there might be some other possible way of getting relief for the losses which, despite making reasonable enquiries of German and Belgian tax specialists, it has not thought of and therefore has not eliminated.”

19. The judge then turned to the question: “What is the relevant time as at which M&S has to demonstrate that the conditions of paragraph 55 were satisfied in relation to the losses of [MSG] and [MSB]?”.

He thought that there were three possibilities, which he set out at [43] of his judgment:

> “ [43] … (1) the end of the accounting period of loss for [MSG] and [MSB], and thus also the end of the accounting period of M&S as respects which M&S has claimed group relief for the losses; (2) the time or times when M&S made the claim or claims for group relief; (3) the time when an appeal on the question is decided by the Special Commissioners.”

He concluded that it was the second of those possibilities which provided the answer: the time or times when M&S made the claim or claims for group relief. His reasons are set out at [44] to [46]:

> “ [44] … Time (1) is too soon, and would be likely to rule out virtually every case. At the end of an accounting period in which [MSG] or [MSB] made a loss and therefore was likely still to be carrying on its trade it is hard to imagine any case in which German or Belgian law would not provide for some possibility of relief for the losses.
>
> [45] Time (3) does have the linguistic support that in paragraph 56 of the ECJ judgment the word ‘demonstrates’ is in the present tense, but I do not think that the ECJ meant to say that the paragraph 56 tests fell to be determined only by reference to the circumstances which existed when a case came to appeal, however remote that time was from the underlying events which gave rise to the issue. If that was the position it would mean that a company could claim group relief at a time when relief was not available, but then spin out time before the matter came to appeal in the hope that by then the facts would have changed and the appeal would succeed.
>
> [46] In contrast, time (2) in my view provides a rational basis for applying paragraph 55. If a company claims group relief at a time when the paragraph 55 criteria are satisfied it should get the relief. If it applies for it at a time when the criteria are not satisfied it should not.”

39. It should be noted, in relation to this last point about the time for demonstrating that the no possibility test is satisfied, that Park J had before him only those group relief claims which had been made up to that time (that is, the first group relief claims and the claims made for 1996 and 1997 in relation to MSG); none of the other claims had yet been made.

***M&S*: the Court of Appeal**

40. The Court of Appeal upheld Park J's conclusion that the relevant time at which M&S was required to show that the no possibilities test was satisfied is the time of the making of the claim for group relief. Neither Park J nor the Court of Appeal needed to address the question faced by the Tribunal and now by us on appeal about the making of new claims in respect of the same losses at times when the facts relevant to the satisfaction of the test may have changed. HMRC's position on the timing point before Park J and in the Court of Appeal was that the time at which it has to be demonstrated that there was no possibility of utilising the losses locally was the end of the accounting period in which the losses accrued. They reserve that position for a higher court but accept that, before us, we must apply the decision of the Court of Appeal on that point.

41. The Court of Appeal also broadly endorsed the guidance which Park J had provided by reference to the examples which he had given. In relation to what the Judge had said at the end of paragraph 37 of his judgment Chadwick LJ said this:

> "[48] The judge was clearly correct, if I may say so, to recognise that a possibility can exist even if it is unlikely that it will ever happen. It is, I think, plain that the Court of Justice did not intend that the test posed by the second of the para 55 conditions would be satisfied if the claimant did no more than demonstrate that it was improbable or unlikely, or that there was little or no real likelihood, or that the claimant (or the surrendering company) had no intention, that losses could or would be set against future profits. In my view the examples which the judge gave cannot be said to be flawed. The danger, I think, is that more may be read into the judge's observation that 'the particular circumstances of [MSG] and [MSB] do not for these purposes include the degree of probability or improbability of them returning to profitability' than, perhaps, he intended.

42. The language used by the ECJ in identifying the two limbs of the no possibilities test is slightly different. A textual analysis might therefore suggest that the ECJ was applying a different approach to each limb – a factual analysis to the first limb with a more theoretical approach to the second limb. However, Chadwick LJ rejected that suggestion:

> "[49] In my view M&S is correct in its contention that there is no reason to think that the test under the second condition is of a different nature from that under the first; that is to say, that there is no reason why the test under the second condition should not have regard to 'the objective facts of the company's situation at the relevant time'. So that, if on an objective appraisal of the surrendering company's situation, the proper conclusion is that there is no real possibility for losses incurred in the surrender period to be taken into account in its state of residence for future periods, either by the surrendering company or by a third party, then the second of the para 55 conditions is satisfied. Given the context, the phrase 'no possibility' in the second condition

is to be read as 'no real possibility'; in the sense that a real possibility is one which cannot be dismissed as fanciful. It is, perhaps, unnecessary to add that a test of 'no real possibility' is not to be equated with a test of 'little or no real likelihood'. As I have said, the judge was correct in his view that a possibility may exist even where there is little or no real likelihood that the event will happen."

43. Chadwick LJ also addressed submissions made on behalf of M&S which went beyond those which had been addressed to Park J. The first of those related to the Community law principle of effectiveness. It was said, as Chadwick LJ summarised the submission, that this principle requires that the period during which M&S is permitted to make a claim for group relief— and to demonstrate that, at the time when the claim is made, there is no possibility that the losses of the surrendering company will be used in the state of residence— be extended so far as necessary to allow a claim for relief to be made within a reasonable time after the date on which its Community right to make group relief claims in respect of non-resident subsidiaries was established. This was probably the date of the decision of ECJ in *M&S* although M&S keeps open the possibility that it is a later date being the date on which " it is made aware of the precise nature of [the para.55] requirements". M&S relied, in support of that submission, on observations in the Court of Appeal in *Condé Nast Publications Ltd v Customs and Excise Commissioners* [2006] EWCA Civ 976, in particular at paragraph 49. That decision has since been the subject of an appeal to the House of Lords.

44. In paragraph 54 of his judgment, Chadwick LJ then said this:

"54 For my part, I would accept that the decision of this Court in *Condé Nast* does provide support for the proposition that the Community law principle of effectiveness requires that the period during which M&S is permitted to make new claims for group relief be extended so far as necessary to allow those claims to be made within a reasonable time after December 13, 2005. If M&S is permitted to (and does) make a new claim (or claims) for group relief, then it follows from the conclusion that I have reached earlier in this judgment that M&S will have the opportunity to demonstrate that, on the facts as they are at the date that the new claim (or claims) is or are made, there is no possibility that the losses of the surrendering company will be used in the state of residence."

45. We will return to consider further the principle of effectiveness and its possible application in the present case later in this Decision.

46. Before leaving the decision of the Court of Appeal, we note the observations of Chadwick LJ in paragraph 41 of his judgment:

"The ruling of the Court of Justice requires, as it seems to me, that in cases where the restrictions on group relief in respect of the losses of non-resident companies go beyond what is necessary in the pursuit of legitimate objectives compatible with the EC Treaty, those losses are to be treated, so far as possible, in the same way as losses of resident companies. Differential treatment is to be avoided. The decision of a resident company to surrender its losses – and to give notice of consent – can be made at or up to the time when the claimant company makes its claim for group relief; and so can be made on the basis of facts as they are at the end of the period within which the claimant company is permitted to make a claim for group relief. It is, I think, plain that the decision of a non-resident company to surrender its losses – because they cannot be used in its own state of residence – can be made at or up to the time when the claimant company makes its claim for group relief. I can see no reason why that decision, also, should not be made on the basis of facts (including facts which go to the question whether or not the para 55 conditions are satisfied) as they are at the end of the period within which the claimant company is permitted to make its claim."

47. Although he said this in the context of arguments about the time for applying the no possibilities test, we see no reason to think that it is other than the correct approach to all aspects of the claim for group relief in relation to a foreign subsidiary's losses. Differential treatment is to be avoided. Accordingly, if group relief claims in respect of a UK subsidiary are subject to substantive or procedural conditions, those conditions should apply in a similar way in respect of a foreign subsidiary subject always to compliance with the principle of effectiveness. Correspondingly, where those conditions give flexibility, in the domestic context, for the making of a group relief claim during the course of the period within which a claim is permitted, such flexibility should be available throughout that period in the different circumstances in which a claim can be made for losses of a foreign subsidiary.

Some features of the no possibilities test

A. An all or nothing test?

48. One issue which arises is whether the no possibilities test has to be satisfied in relation to the whole of the subsidiary's loss for the accounting period or whether it applies to each euro of loss separately. Suppose that the subsidiary has a loss of €10,000; it has exhausted the local provisions for utilising that loss; but it still has €8,000 unrelieved. Of that figure it can be said, on the facts, that there is no possibility of €5,000 ever being used in the subsidiary's home Member State but €3,000 might be relieved in the future. Mr Ewart argues that, because part of the loss might be used in the future, the no possibilities test is not fulfilled in relation the loss as a whole and that it is no answer to say that it is fulfilled in relation to part of the loss.

49. We disagree with that approach, as did the Tribunal. Taking it to an extreme (but not *de minimis*) case, the possibility of being able to use €10,000 of a €1 million loss would, on Mr Ewart's approach, disqualify the entire loss from relief. We cannot see a rational basis for such a result. Indeed, the ECJ's reason for introducing the no possibilities test was to ensure that provisions such as UK group relief which pursue a legitimate objective do not go beyond what is reasonably necessary to obtain that objective. It would go beyond that objective to refuse group relief in respect of part of a loss which fulfilled, viewed by itself, the no possibilities test.

B. How to apply the no possibilities test at the time of the claim

50. The next issue relates to the time when the no possibilities test has to be fulfilled. Park J and the Court of Appeal held that the correct time for deciding whether the no possibilities test is satisfied is the time when the claim is made. In order to understand just what they did decide, it is necessary to go back to how Chadwick LJ described the competing positions of M&S and HMRC. At paragraph 32 of his judgment, he said this:

> "32 The issue between the parties, however, is not as to the time at which the claimant company must seek to demonstrate that the para.55 conditions are satisfied; but rather as to the time at which those conditions are, in fact, to be satisfied. In other words, is it enough (as the judge held and as M&S contends) that the conditions are satisfied at the time when the claimant company makes the claim for group relief; or must it be demonstrated at the time when the claim is made (as the Revenue contends) that the conditions were satisfied at the end of the accounting period for which group relief is claimed?"

51. Although this appears to be a dichotomy, it hides more than two possibilities. There are really three that need to be borne in mind. We find it easiest to explain this by reference to an example,

52. Imagine, therefore, a surrendering company, S, as follows:

    a. S has losses of €100,000 for the accounting period in question. Call the end of that accounting period time T1.

    b. S makes a claim for group relief for the losses of that accounting period at time T2. By that time, it has exhausted all the local reliefs available in respect of the accounting period in question (i.e. the year ending at T1) and in so doing has utilised €20,000 of such losses.

    c. In the period from T1 to T2, by carrying forward the losses it has used a further €10,000 of losses, locally exhausting all the reliefs available to it for the period up to T2.

    d. It can be said with certainty that S will be unable to utilise the unused losses locally at any time after T2.

53. HMRC's argument had been that the time at which the no possibilities test had to be fulfilled was T1. In other words, looking at the facts as they stood at T1, could it be said that the test was satisfied? This was in accordance with a literal reading of the words used in the ECJ Judgment. As we have said, the no possibilities test has two limbs:

    a The first limb looks backwards and asks, for the relevant accounting period and earlier periods, whether the surrendering company has exhausted it opportunities for using the losses. In that context, it will be remembered that one legitimate objective of the group relief provisions was to prevent a subsidiary transferring its losses to a tax zone with a higher rate of tax than locally; such transfers should be permitted only where the use of the losses locally had been exhausted.

    b The second limb looks forward, referring to future periods which one might think was a reference to any period after the accounting period in question. In other words, it is any period after T1.

    One might think, therefore, that the ECJ had in mind a test which fell to be applied at the end of the accounting period in which the losses accrued: to determine whether in that current period or prior periods losses had been utilised (the first limb); and whether any unutilised losses could possibly be used in subsequent accounting periods (the second limb).

54. Park J and the Court of Appeal rejected that conclusion and held that, at least in the context of the UK scheme of group relief, the time for considering whether the conditions of the no possibilities test are satisfied is the time of the claim.

55. It is worth setting out what Chadwick LJ said about this at paragraph 36 of his judgment:

> "36. …It is important to keep in mind, as it seems to me, that the question whether the United Kingdom tax authorities are precluded by Community law from applying the restriction on group relief imposed by domestic law does not arise until a claim for group relief is made by the claimant company….The question whether the UK tax authorities are precluded by Community law from applying the restriction on group relief imposed by domestic law turns on whether the para.55 conditions are satisfied. I can see no reason in principle why the latter question— whether the para.55 conditions are satisfied— should not be answered by reference to the facts as they are when the former question arises."

56. It is clear from that that one is to have regard to the facts as they stand when the group relief claim is made. If at that time it is known, when it was not known at the end of the accounting period, that no further local relief is possible, then the no possibilities test may be fulfilled. There are, however, two interpretations of what he and Park J meant when they said that the conditions must be fulfilled at the time when the claim is made:

> (1) The first is that they intended to apply to the situation as it is found at time T2 the reasoning which led to the no possibilities test. In other words, they ask whether all the available local reliefs have been utilised up to the date of the claim, T2, and apply the second limb from that time. We then find that €30,000 of losses have in fact been utilised and the possibilities have been exhausted not only up to time T1 but to time T2; and we find (*ex hypothesi*) that there is no possibility of utilisation.
>
> (2) The second is to look at the position as it would have been at time T1 but with the benefit of the knowledge of what has in fact happened in the period T1 to T2 and with the knowledge of no possibility of utilisation after T2. In other words, the facts as they are known at T2 are to inform the answer to the question whether the no possibilities test was fulfilled at the end of the accounting period.
>
> This second approach leads to the same conclusion as the first approach, but depends on the correctness of our view that the no possibilities test is to be applied on a euro by euro basis as already discussed. If we were wrong about that, then knowledge of what has in fact happened would not be enough to bring the no possibilities test into play. This is because it would be known at T2 that a person judging the matter at T1 would know that some of the losses would in fact be used in the period T1 to T2 and so would know that the no possibilities test was not fulfilled at time T1

57. Neither of these approaches sits entirely comfortably with a literal reading of what the ECJ said. But once it is accepted, as it has to be, that the time when the conditions of the no possibilities test is fulfilled is not the end of the accounting period, a literal reading has to be abandoned. In any case, we have little doubt

that had the ECJ addressed the issue which we are addressing, it would have adopted one or other of those two approaches and would have reached the conclusion which we have reached. We think it is important, too, to observe that the ECJ was required to deal with this point in terms of general principles which are likely to be required to apply in a variety of group relief, loss consolidation and other schemes in different Member States for relieving losses between group companies, and that in any particular Member State it is for the national court to apply those principles pragmatically in a way which is consistent with the workings of the local scheme in the local context.

The validity of the group relief claims made by M&S

58. If the question is whether, at the time the group relief claim was made in respect of the MSG and MSB losses, there was then no possibility of those losses being utilised locally, it is necessary to ascertain when M&S made the group relief claim which gives rise to that enquiry. The particular difficulty of this case is that, as explained, M&S made a series of group relief claims in relation to the losses, and it is possible that, posing the no possibilities test at the time of each of those different claims, different answers will ensue. This was not a matter which required consideration by Park J or the Court of Appeal, since at the time of those cases only the first group relief claims had been made (together with the first claims for the years 1996 and 1997 in relation to losses of MSG). The Tribunal decided that, at the time that the first group relief claims were made, and notwithstanding that MSG and MSB had by then ceased trading, there was a possibility that the losses accrued in the relevant years could be utilised locally (if, for example, the trade had been recommenced or another trade undertaken), so that had matters rested there, M&S could not have claimed those losses by way of group relief (before us M&S argued, as an alternative case, that the Tribunal was wrong in its decision on this point). But matters did not rest there, since M&S went on to make further group relief claims to take account of both the import of the ECJ Judgment and the subsequent UK litigation and also the action taken to liquidate and dissolve the foreign subsidiaries.

59. As mentioned, different group relief provisions apply for the pay and file years (for M&S, the years up to and including 1999) and the self-assessment years (2000 to 2002). We propose to follow the Tribunal's approach of dealing first with the self-assessment years and then return to the pay and file years.

60. In the Tribunal's Substantive Decision (at paragraph 22(1)) the Tribunal made findings of fact as to the group relief claims made by M&S in relation to losses of MSB for the year ended 31 March 2000, finding, further, that the claims made in relation to those losses were typical of the claims made in relation to losses of MSB in other years and the losses of MSG in each of the self-assessment years. The Tribunal's findings are as follows:

> "We find the following further facts about the claims and the liquidation of the companies:
>
> (1) Taking the MSB claims for the year ended 31 March 2000 as an example:
>
> (a) the first group relief claim was made on 24 September 2001 for £3,346,511 (€5,230,597). The consent was to surrender that euro figure to

the appellant 'or such higher or lower amounts that may be agreed which were incurred during the accounting period ended 31 March 2000.'

(b) the second group relief claim was made on 20 March 2007 and was for the different figure of €4,797,410. It was stated to be a new claim in addition to and not in substitution for the first group relief claim which was not withdrawn. It was made subject to any adjustments required to give effect to the Judgment of the ECJ. The letter also said:

> 'This claim is made without prejudice and in the alternative to the Original Claim for 2000 Belgian losses. The Claimant does not seek group relief twice for the same profits and losses for the same accounting period. Rather in so far as it is required to meet conditions to make group relief claims in respect of the non resident losses of non resident subsidiaries (such as those referred to in paragraphs 55 and 56 of the judgment of the European Court of Justice in C-446/03 *Marks & Spencer plc v Halsey*), the claimant is entitled to claim that it does meet those requirements either at the time and in the manner required as part of the Original Claim for 2000 Belgian losses and/or as part of this claim (see *Halsey (HMIT*) *v Marks & Spencer, Marks & Spencer v Halsey* (HMIT) supra at paragraphs 51 and 55.
>
> If upon determination of the Original Claim for 2000 Belgian losses it is found that all necessary conditions are met and that claim for group relief is allowed, then the Claimant hereby undertakes forthwith thereafter to withdraw this claim. If upon determination of this claim it is found that all necessary conditions are met and this claim for group relief is allowed, then the Claimant hereby undertakes forthwith hereafter to withdraw the Original Claim for 2000 Belgian losses. If both claims are allowed, the Claimant hereby undertakes forthwith thereafter to withdraw that claim which permits the surrender of the least losses, or if in the same amount, this claim."

The accompanying surrender was for €4,797,410 likewise subject to any necessary adjustments.

(c) the third claim was made on 12 December 2007 and was in the same form as the second claim (the covering letter made reference to the second claim), as was the surrender.

(d) the fourth claim was made on 11 June 2008 in the same form as the second and third claims except that it did refer to the previous claims, as was the consent to surrender which the liquidator signed on 31 March 2008 and which confirmed the conclusion of the liquidation on 27 December 2007."

61. In relation to the group relief claims for the self-assessment years the Tribunal reached the following decisions (at paragraphs 36 – 40):

(1) In respect of both MSG and MSB, at the time the first group relief claims were made the losses for the relevant years did not satisfy the no possibilities test and therefore could not be claimed by M&S by way of group relief;

(2) Therefore M&S could not have made a valid claim for group relief at that time and so the first group relief claims were a nullity;

(3) If, to the contrary, the first group relief claims have some validity, M&S has undertaken to withdraw them, and is entitled to do so, whereupon they will cease to have effect. M&S will then be at liberty to make new claims which it is still in time to do under the self-assessment rules;

(4) The second group relief claims are different from the first group relief claims because they were for different specified amounts of losses claimed;

(5) In respect of both MSG and MSB, at the time the second group relief claims were made the losses for the relevant years did satisfy the no possibilities test and therefore M&S could claim those losses by way of group relief;

(6) Therefore the second group relief claims were valid claims;

(7) If the Tribunal were wrong, and at the time the second group relief claims were made the losses did not satisfy the no possibilities test, then the second group relief claims must, like the first group relief claims, be invalid. In that situation, at the time the third group relief claims were made the losses for the relevant years satisfied the no possibilities test and therefore M&S could claim those losses by way of group relief by means of the third group relief claims;

(8) In relation to the losses of MSB, if all previous group relief claims were invalid because when those claims were made the losses did not satisfy the no possibilities test, the Tribunal would have allowed M&S to call evidence on the powers of the liquidator in Belgium in the expectation that the liquidator had power to give the consent he gave on 11 June 2008 to the surrender of losses in which case the fourth group relief claim would be valid.

62. By way of further preliminary point we should mention again that, in relation to the self-assessment years, all the group relief claims made by M&S were made within the period specified by the group relief provisions for the making of valid claims (but, as will appear, this is not the case in relation to the pay and file years).

63. HMRC's position is that the first group relief claims are both valid and sufficient, and that the second, third and fourth group relief claims are not valid claims at all, whether as a matter of domestic law or for the purposes of the application of the no possibilities test as a matter of Community law. M&S's position, in stark contrast, is that if the first group of claims are not valid claims at all, the result is that those claims did not have to be withdrawn before the later claims could be made. Accordingly, the later claims are valid and are, in any event, distinct and different claims in their own right.

64. There are at least two issues lurking in these different positions. The first is whether, as a matter of purely domestic law, a claim for group relief for a specified sum is an invalid claim, or if we might use the phrase, a "non-claim", when, following an investigation of the facts, the specified sum allowable is reduced to nil. The second issue is whether, if, in a case where there is a Community law right to group relieve foreign subsidiary losses, an original claim is validly made as a matter of domestic law, Community law allows a subsequent

claim to be made without the first claim having been withdrawn in order to give effect to the right to group relieve those losses when that right becomes exercisable (provided any such subsequent claim is made within time limits imposed by domestic law).

Were the first group relief claims valid claims?

65. The importance of the answer to the question whether the first group relief claims were valid is this. If they were invalid, or non-claims, then they can be ignored and the second, third and fourth group relief claims can be looked at on their own merits. But if they were valid, HMRC submit, in relation to the self-assessment years, that further claims could not be made unless and until the first group relief claims had been withdrawn (M&S had, in making the subsequent group relief claims, undertaken in certain circumstances to withdraw earlier claims, but had not done so). The sting in the tail is that, in HMRC's submission, if the first group relief claims are withdrawn, the later claims are invalid for a variety or reasons including (i) the later claims would not be effectively made until withdrawal of the earlier claims and may then be out of time and (ii) the later claims simply repeat the earlier claims and their validity should be judged by reference to whether the no possibilities test was satisfied when the original claims were made.

66. In dealing with these questions in relation to the self-assessment years we propose to look at the structure of sections 402 and 403 ICTA 1988 together with Schedule 18 FA 1998; and then to consider how these provisions should apply to give effect to M&S's Community law rights (and in that context, to look in more detail at the Community law principle of effectiveness).

The structure of the domestic legislation in relation to self-assessment years

67. We have set out the relevant words of section 402(1) and section 403(1). Those set out the broad parameters of the relief and leave the detail of how claims are to be made to other provisions, now Schedule 18 FA 1998. Thus section 402 provides that amounts eligible for relief may be surrendered by one company and allowed to another company on the making of a claim by it. Section 403 specifies the types of losses or deductible items of the surrendering company which are eligible for surrender by way of group relief and provides that the amount of such losses or items may be set off against the profits of the claimant company for its corresponding accounting period.

68. There is nothing in those sections which restricts a surrendering company to making only one surrender or a claimant company from making only one claim. Indeed, it is quite clear from both Schedule 17A ICTA 1988 (pay and file) and Schedule 18 FA 1998 (self-assessment) that a surrendering company may surrender part of its losses to one claimant company and part to another; and equally it is clear that different surrendering companies may surrender losses to the same claimant.

69. For self-assessment years, the detail is provided in Schedule 18 FA 1988. Some care needs to be taken over terminology. The word "claim" appears both in section 402 and in various paragraphs of Schedule 18. In the section, "claim" is being used in the sense of asking for a relief which the statute provides: unless the request is made, the relief is not given. One cannot of course claim, in that sense,

something to which one is not entitled. But if one claims that to which one is entitled in principle but overstates the amount, it may nonetheless be a claim, albeit one which cannot be allowed as to the excess.

70. This is reflected in Schedule 18. It provides in paragraphs 67 and 68 how the "claim" provided for by sections 402 and 403 is to be made. The claim is made in the tax return of the claimant and is reflected also in the tax return of the surrendering company. This reflects the underlying approach of group relief claims in a system of self-assessment, where the taxable entities (the group companies) submit their completed returns to include all reliefs claimed and showing the resulting tax which they assess is due. As will be apparent, a system of claiming group relief based on tax returns submitted does not readily fit with the circumstances of claiming relief for foreign subsidiary losses where the foreign subsidiary will not be filing a UK tax return.

71. In addition to the inclusion of claims and surrenders in the tax returns of the claimant and surrendering companies, for a claim to be effective the surrendering company must notify HMRC of its consent to the surrender, specifying the required information including the amount of relief being surrendered and the claimant company: paragraphs 70 and 71. Consistent with the underlying self-assessment approach, if the surrendering company gives its notice of surrender after if has submitted its tax return, it must amend its return so as to reflect the notice of consent (i.e. to show that the losses in its return have been surrendered by way of group relief): paragraph 72. The notice of consent provisions seem designed simply to ensure that HMRC can relate surrenders and claims when examining the individual tax returns of group companies.

72. The starting point under paragraph 69 is the tax return of the surrendering company since it is by reference to that return that the amounts available for surrender are determined. This is entirely logical: the return is assumed in the first instance to be correct and thus reflects the amounts which are, *prima facie*, available for surrender. There can be no doubt at all that a claim made in accordance with paragraph 69 which claims no more than "the amount available for surrender" (as defined in paragraph 69(3)) at the time of the claim is a valid claim for the purposes of Schedule 18. It may, in the event, turn out to be a claim to more than the claimant is in fact entitled because "the amount available for surrender" may be reduced following an amendment to the tax return of the surrendering company. The lesser amount is the amount in respect of which the claimant is entitled to make a "claim" within section 402; but it makes that claim validly by claiming (in the sense of asking for) an amount not exceeding "the amount available for surrender". So, although the lesser amount is all that the claimant is ultimately entitled to enjoy by way of set off for corporation tax purposes against its total profits, the claimant has made a valid claim within section 402 and not a claim which is ineffective or a non-claim.

73. With that is to be contrasted the position if the claimant claims in its tax return group relief if the relief claimed exceeds "the amount available for surrender". In that case, the claim is ineffective under paragraph 69(2) and does not, therefore, constitute a "claim" within section 402. This deals with the situation where the claimant claims more than the surrendering company shows in its tax return as being available for surrender – not, as the Tribunal considered to be the case, with the situation where the claim was made by reference to the amount which the

surrendering company assumed was available for surrender but where that is subsequently proved to be an over-estimate of such amount or where it is subsequently proved that there are no losses to surrender.

74. It is clear that an amount cannot be utilised twice under sections 402 and 403. Section 403 provides for the set off of the surrendered amounts against the claimant's total profits but it is obviously not possible to set off an amount more than once since, having been set off once, it is simply no longer available. This is reflected in the calculation of "the amount available for surrender", which takes account of previous surrenders under the Second step under paragraph 69(3).

75. The mechanism for making the claim is laid down by paragraphs 67 and 68: it must be made by being included in the claimant company's tax return for the accounting period for which the claim is made. The claim must be for a specified amount which is quantified at the time when the claim is made. In the context of a purely domestic claim, this is a sensible course and is not onerous. The "amount available for surrender" is easily found by an examination of the surrendering company's tax return and by reference to notices of consent already given. It is not unreasonable to expect the two companies concerned to agree precisely (the surrendering company's consent being required under paragraph 70(1)) the amount to be surrendered and to include that amount in the claim for relief as a quantified sum.

76. It seems to us to be clear that, where different companies have surrendered their losses to the same claimant company, the claimant is able to make separate claims in respect of each surrendered amount. There does not need to be a single claim for group relief which would require the claimant to withdraw its existing claim each time a new surrender was made to it by a different surrendering company.

77. Given that a claimant company can make separate claims in relation to different companies, we see no reason in principle why a claimant company should not be able to make separate claims in respect of different amounts surrendered to it by the same surrendering company on different occasions. Suppose that the tax return of a claimant company, C, shows that it has profits of £P1; a subsidiary S has losses of £L1 exceeding £P1. It surrenders £P1 to C. C's tax return is subsequently amended to show a larger profit of £P2. There is no reason why S should not then surrender a further amount to C. So far as we can tell, there is nothing which prevents the surrendering company from surrendering the additional amount without first having to withdraw its original notice of consent: it simply gives a further notice of consent, and amends its tax return if that has already been made. And similarly, there is nothing to prevent the claimant company from making a separate claim in respect of the additional amount surrendered any more than it is restricted to making a single claim in respect of amounts surrendered by different surrendering companies.

78. We are therefore of the view that domestic law does not require a group relief claim by a single claimant in respect of the losses of a single surrendering group company to be made by a single claim. If the surrendering company surrenders its losses sequentially, the claimant company is entitled to make sequential claims, provided the appropriate notices of consent are given and the respective tax returns amended to reflect the changed circumstances. This point, in a domestic context, is unlikely ever to have any significance. Its significance in the context

of the enforcement of M&S's Community law rights will become apparent in due course.

79. Even if that is wrong, and the claimant may make only one claim in relation to any particular surrendering company, it is clearly open, as in the example which we have given, for the surrendering company to make sequential surrenders and give sequential notices of consent. It does not have to withdraw an earlier notice before it can give a subsequent notice. Accordingly, the claimant could withdraw its original claim and make another which subsumed both notices of consent.

80. The legislation takes account, at paragraph 75, of the possibility that the surrendering company's tax return might be wrong. Paragraph 75 applies where the total amount available for surrender is reduced to less than the amounts already surrendered. The surrendering company is then required to withdraw the notices of consent so as to bring the total amount surrendered within the new total amount available for surrender. It must give notice to the claimant company and to HMRC.

81. When the claimant company receives the notice of withdrawal, paragraph 75(5) provides

> "it must, so far as it may do so, amend its company tax return….so that it is consistent with the new position with regard to the consent to surrender."

82. There are two points we would make about that. First, it only has to amend its return so far as it may do so. If time limits for the amendment of a return have passed, the claimant company will have no power to amend (but of course HMRC will in such a case exercise their power to amend the return). Secondly, (and this point is underlined by the first point) there is nothing which would lead to the conclusion that the original claim, viewed as a request for the relief for which section 402 provides, was in any sense invalid or ineffective.

83. As to the second point, the claimant's tax return will have to be amended to reflect the withdrawal of the notice of consent. This will be done by reducing the figure originally set against total profits (pursuant to the group relief claim) by the full amount comprised in that notice. But there is nothing, we think, which requires the claim itself (albeit a claim contained in the tax return) to be amended. Instead, the claim is given effect to in a reduced amount. If the claimant company has received only one notice of consent from the surrendering company and has made only one claim for group relief in relation to it, the amount will be reduced to nil. This does not render the original claim a nullity. It was and remains procedurally valid albeit that the set off provided for under section 403 is reduced to nil and even though it can then be seen that there was, in the eventual outcome, no relief in respect of which a "claim" could be made for the purposes of section 402.

84. Even if, contrary to our view, the claim itself had to be amended to reflect the withdrawal of consent, that would still not make the claim as originally made in accordance with Schedule 18 invalid or even ineffective. It would simply have the result that the claim had to be withdrawn. That does not mean it was not valid or effective when made. A similar analysis applies for the purposes of paragraph 71(5) which applies where a notice of consent is withdrawn by the surrendering company with the consent of the claimant company, requiring the claimant company to amend it tax return to reflect the changed circumstances.

85. There is also this important point to note. A notice of consent has to be withdrawn in whole: it cannot be withdrawn in part by way of amendment. Accordingly, a reduction in the total amount available for surrender may trigger the need to withdraw a notice of consent which relates to a higher figure than the reduction which triggered the withdrawal. Take the simple case of a single consent to surrender a loss of £100 being the loss shown in the surrendering company's tax return. The return may be adjusted to show a loss of £90, requiring the withdrawal of the notice of consent. The surrendering company can then give a new notice of consent under paragraph 75(2). It could not possibly be argued, we think, that a claim for group relief based on that new consent would be invalid because it simply repeats an earlier claim which had been withdrawn.

86. Our overall conclusion with regard to the group relief provisions as they apply in the domestic context under the self-assessment regime is that, whilst they are detailed and prescriptive, they are nevertheless both flexible and dynamic: in broad terms, the "mechanics" of Schedule 18 FA 1998 are directed so as to achieve the result that, in their final form, the tax returns of the claimant and surrendering companies accurately reflect amounts eventually shown to be available for surrender, as supported by corresponding notices of consent. Further, the processes and adjustments required to reach that final result may continue throughout the period during which it is open for a group company to make a group relief claim (which in practice, under self-assessment, is a generous period). That is all that is required in a self-assessment regime, and the flexibility and dynamism are required where, in large groups of companies with complex tax affairs, adjustments and consequential changes are likely to be inevitable and frequent.

Application of UK requirements to Community law claims

A. The case law

87. In order to give effect to M&S's Community law rights, some adjustment or remoulding of the domestic legislation is required. Lord Nicholls put the matter this way in *Autologic plc v Inland Revenue Commissioners* [2006] 1 AC 118:

> "16 The second basic principle concerns the interpretation and application of a provision of United Kingdom legislation which is inconsistent with a directly applicable provision of Community law. Where such an inconsistency exists the statutory provision is to be read and take effect as though the statute had enacted that the offending provision was to be without prejudice to the directly enforceable Community rights of persons having the benefit of such rights. That is the effect of section 2 of the European Communities Act 1972, as explained by your Lordships' House in *R v Secretary of State for Transport, Ex p Factortame Ltd* [1990[2 AC 85 ,140, and *Imperial Chemical Industries plc v Colmer* (No 2) [1999] 1 WLR 2035 , 2041.
>
> 17 Thus, when deciding an appeal from a refusal by an inspector to allow group relief the appeal commissioners are obliged to give effect to all directly enforceable Community rights notwithstanding the terms of sections 402(3A) and (3B) and 413(5) of ICTA . In this regard the commissioners' position is analogous to that of the *Pretore di Susa in Amministrazione delle Finanze dello Stato v Simmenthal SpA* (Case 106/77) [1978] ECR 629. Accordingly, if an inconsistency with directly enforceable Community law exists, formal

statutory requirements must where necessary be disapplied or moulded to the extent needed to enable those requirements to be applied in a manner consistent with Community law. Paragraph 70 of Schedule 18 to the Finance Act 1998 is an instance of such a requirement. Paragraph 70 provides that a claim for group relief requires the consent of the surrendering company, which must be given by notice in writing to its own inspector of taxes when or before the claim is made. This provision cannot be applied literally in the case, say, of a German subsidiary which makes no tax returns in this country. So if the residence restriction is found to be inconsistent with Community law this provision will need adapting so as to give effect to the overriding Community rights. In this regard the appeal commissioners have the same powers and duties as the High Court.

88. The disapplication or the moulding referred to by Lord Nicholls must, of course, result in the principle of effectiveness being complied with. That principle is not restricted to time limits. The principle applies as much to the moulding of the statute as it does to the procedural requirements for enforcing the Community law right. The statutory conditions, after relevant disapplication or moulding, must result in proper recognition of the Community law so that the right is not practically impossible or excessively difficult to exercise.

89. The Crown had relied on the decision of the ECJ in the case commonly referred to a *Hoechst* but more fully cited as *Metallgesellschaft Ltd v Inland Revenue Comrs; Hoechst AG v Inland Revenue Comrs* (Joined Cases C-397 and 410/98) [2001] Ch 620; [2001] 2 WLR 1497; [2001] ECR-I 1727. We think it is worth setting out a few paragraphs of the decision:

> "104 Finally, the orders for reference make it clear that an appeal against such a refusal by the tax authorities could have been brought before the Special or General Commissioners and then, if necessary, before the High Court. According to the national court, before judgment could be given in such an appeal, the subsidiaries would still have had to pay ACT in respect of all the dividends which they had paid out and, furthermore, if the appeal had succeeded, they would not have obtained reimbursement of the ACT, since no such right to reimbursement exists under English law. If the subsidiaries had chosen not to pay ACT in respect of dividends paid before the determination of their appeals, they would nevertheless have been assessed to ACT, would have had to pay interest on those sums and would have laid themselves open to statutory penalties if they had been judged to have acted negligently and without reasonable cause.
>
> 105 It therefore appears that, in the cases in the main proceedings, the United Kingdom Government is blaming the plaintiffs for lack of diligence and for not availing themselves earlier of legal remedies other than those which they took to challenge the compatibility with Community law of the national provisions denying a tax advantage to subsidiaries of non-resident parent companies. It is thus criticising the plaintiffs for complying with national legislation and for paying ACT without applying for the group income election regime or using the available legal remedies to challenge the refusal with which the tax authorities would inevitably have met their application.

> 106 The exercise of rights conferred on private persons by directly applicable provisions of Community law would, however, be rendered impossible or excessively difficult if their claims for restitution or compensation based on Community law were rejected or reduced solely because the persons concerned had not applied for a tax advantage which national law denied them, with a view to challenging the refusal of the tax authorities by means of the legal remedies provided for that purpose, invoking the primacy and direct effect of Community law.
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> 107 The answer to the fifth question must therefore be that it is contrary to Community law for a national court to refuse or reduce a claim brought before it by a resident subsidiary and its non-resident parent company for reimbursement or reparation of the financial loss which they have suffered as a consequence of the advance payment of corporation tax by the subsidiary, on the sole ground that they did not apply to the tax authorities in order to benefit from the taxation regime which would have exempted the subsidiary from making payments in advance and that they therefore did not make use of the legal remedies available to them to challenge the refusals of the tax authorities, by invoking the primacy and direct effect of the provisions of Community law, where upon any view national law denied resident subsidiaries and their non-resident parent companies the benefit of that taxation regime."

90. The taxpayer in *Autologic* had relied on this ruling. In relation to that, Lord Nicholls had this to say:

> "[29] ……The taxpayers' reliance on this ruling in the present cases is misplaced. The taxpayers are seeking to apply the European court ruling out of context. In the Hoechst case this ruling was directed at rejecting a governmental defence based on the taxpayers' alleged lack of reasonable diligence in pursuing its claims. The Hoechst ruling was not directed at a situation where, as here, the claimants' claims have yet to be decided by the national court and there exists a statutorily prescribed route by which the claimants are able to obtain the tax relief they say is their entitlement under Community law. Which court or tribunal has jurisdiction to hear disputes involving rights derived from Community law is a matter for determination by each member state…."

91. But he went on to explain that it was necessary ensure that the statutory code is applied in such a way as provides an effective remedy. He said this:

> "[30] Of course, to be compliant with Community law the remedial route prescribed by the legal system of a member state must be such that the rules 'are not less favourable than those governing similar domestic actions (principle of equivalence)' and, additionally, the rules must not render 'practically impossible or excessively difficult the exercise of rights conferred by community law (principle of effectiveness)': see the Hoechst case, para 85. The statutory route prescribed for group relief claims was not designed for claims in respect of non-resident companies. So, as United Kingdom law presently stands, at the initial step a taxpayer's group relief claim will inevitably be refused by the Revenue. Further, as already noted, some statutory requirements will need adaptation to accommodate claims in respect

> of non-resident companies. But neither of these features should present any major problem. Neither of them renders the statutory route 'practically impossible or excessively difficult'. Adaptation of the formal requirements will be needed whichever route is followed, and the appropriate adaptation is a matter on which the Special Commissioners' practical expertise will be invaluable."

92. As to the necessary remoulding, there are two levels at which this issue needs to be examined. The first is at the general level, giving effect to Community law rights once the no possibilities test had been identified as the touchstone for the entitlement to group relief. The second is at the specific level of M&S (and, if there are any, other taxpayers which had made claims of some sort within the relevant UK time limits but whose claims went further than was permitted by the no possibilities test), the question being whether some transitional relief is to be afforded – although, as will become apparent, this is more of an issue for the group relief claims made in relation to the pay and file years than those made in relation to the self-assessment years.

B. The general level

93. We take the general level first. In this context, we wish to draw an important distinction between the group relief claims where the surrendering company is a member of a UK group and those where the surrendering company is a foreign company.

94. In the case of the UK surrendering company, the claimant company has an easy task to perform. It looks simply to the tax return of the UK surrendering company and its own tax return and the corresponding notice or notices of consent; it tailors its group relief claim by reference to objective and easily ascertainable figures in those returns. There is no element of judgment. If either of the tax returns is amended, the mechanical process for adjusting (and reclaiming) the relief is easy to carry out. Further, it makes little difference when the claim is made provided that it is within the statutory period for doing so (although it will, we acknowledge, have an impact on precisely when the relief is given and may thus have an effect on the cash-flow of the group). The point is that, during the statutory period allowed for making a claim, the claimant company does not have to take care about the precise time when it makes the claim since the possibility of making a claim will not change over of a period of time (subject to potential changes in the surrendering company's tax return).

95. In contrast, there is much more difficulty in relation to the case of the foreign surrendering company. The ascertainment of the amount available for surrender is not a mechanical process derived from a tax return in the way that it is for the UK surrendering company. There is room for judgment about whether the no possibilities test is satisfied. Accordingly, the claimant has to assess whether the no possibilities test is fulfilled and, if so, in respect of how much of the losses of the foreign company. That may give rise to difficult questions of the sort which, in the UK context, would be dealt with in addressing the contents of the UK surrendering company's return (either in negotiation with the tax inspector or on an appeal to the Tax Tribunal). Further, in contrast with the situation of a UK

surrendering company, whether or not a loss, or part of a loss, can be claimed may, during the course of the period in which a group relief claim can be made, change as time passes because the no possibilities test may become fulfilled when previously it was not.

96. In this context, we mention paragraph 69(2) (which we will consider in more detail in a moment). HMRC submit that paragraph 69 is simply to be ignored in the case of a foreign surrendering company. In contrast, M&S submits that if the no possibilities test was not met at all at the time of a claim, the claim is ineffective either because it fails completely on account of not meeting an essential condition for the claim or because it exceeds the amount available for surrender, referring to paragraph 69(2). Implicit in the second reason, we think, is the suggestion that paragraph 69(2) is to be read (or moulded as we would say) so that "the amount available for surrender" is to be equated with the amount in respect of which the no possibilities test is satisfied when the claim is made. One consequence of that suggestion is this: if a claimant pitches its claim a single euro too high, paragraph 69(2) results in the whole claim being "ineffective". That might be thought to be a surprising result. The UK legislation, on this reading, thus puts in the way of the Community law claim a procedural hurdle – the claim must be for a specific amount not exceeding the amount available for surrender - which is not faced in respect of the purely domestic claim.

97. Clearly some moulding of sections 402 and 403 and of Schedule 18 in general and of paragraphs 68 and 69 in particular is required if the provisions are to operate in the case of a foreign surrendering company with the pragmatic flexibility and fluidity with which, as we have already observed, they operate in a purely domestic situation.

98. The requirement in section 402 that the surrendering company be resident in the UK (or non-resident but trading in the UK) must be disapplied altogether. For a UK company, the amount of the "relief for trading losses and other amounts eligible for relief from corporation tax" is ascertained under section 403. In the case of a foreign company the words "relief from corporation tax" are inapposite; further, group relief is not given in relation to all of the foreign company's losses, but only for those which satisfy the no possibilities test. The amount which can be surrendered is to be ascertained under section 403 (appropriately moulded). We think that the phrase "relief….corporation tax" is then to provide for an amount of group relief ascertained by reference to section 403.

99. Section 403 must be modified in two ways. The first is to adapt its provisions so that it identifies the relevant losses which can be taken into account before applying the no possibilities test. The amount of these losses is a matter of some difficulty which is dealt with in the later part of this Decision dealing with quantum. Although the Tribunal has given an answer to the question of the amount available for relief and although we shall do the same, it will not be until the end of the appeal process (perhaps going as far as the Supreme Court) that the parties will have certainty about the amount, if any, which can properly be allowed by way of group relief.

100. The second is to restrict the amount which may be set off against the claimant company's total income to that part of the loss which satisfies the no possibilities test. In contrast with a purely domestic case, this amount is one which can change over time as the no possibilities test becomes fulfilled in respect of losses when previously it was not. It seems to us that the interpretation of these provisions must take account of, and allow for, that factor.

101. We therefore consider that sections 402 and 403 (as moulded to give effect to the Community law right to group relieve losses of a foreign group company) viewed apart from Schedule 18, would allow the making of more than one group relief claim by the claimant company. To put that point a different way, it would not be inconsistent with those sections for a differently worded Schedule setting out the mechanism for group relief claims in relation to the losses of a foreign surrendering company to allow sequential claims. Similarly, it would not be inconsistent with those sections for such a Schedule to provide (i) for the claimant company to make a claim for a specified amount (based on its assessment of the extent to which the no possibilities test was then fulfilled) (ii) for HMRC to substitute a lesser figure if it considered the claim to be too large and (iii) for any dispute about the substituted figure to be resolved in the ordinary way by way of an appeal to the Tax Tribunal. The figure emerging at the end of that process would be the correct figure under section 403 and relief would be allowed in that figure in accordance with the claimant company's rights under section 402. The original claim (for the excess amount) would be a perfectly valid "claim" for the lesser amount under section 402.

102. However, if the amount available is in fact nil, because the no possibilities test was not satisfied, at the time of the claim, in relation to any part of the losses purportedly surrendered, it can be seen, once that fact is established, that there was no right to any relief in the first place. There can therefore be no valid "claim" within section 402. But that does not necessarily mean that a claim for relief, thought by the claimant company and the surrendering company to be valid for the amount claimed but turning out to be unavailable, was procedurally a non-claim any more than in a purely domestic case where an adjustment to the surrendering company's tax return results in there being a nil amount available for surrender.

103. Further, there is nothing in sections 402 or 403, in our view, which would preclude such a new Schedule expressly permitting the claimant to withdraw a claim and then to make a new claim in respect of the same loss; indeed, that can be done in a purely domestic situation. There is nothing in those sections which freezes the claimant's rights by reference to the facts at the time of the first claim. In other words, if a claim is withdrawn (for instance because there is a doubt about the satisfaction of the no possibilities test at the time of the claim) there is no reason why another claim should not be made once it becomes clear that the test is satisfied provided, of course, that such later claim is made within the time limit for making claims. The claims are different, being based on different facts, and we see no reason why a claimant company should prejudice its ultimate position by making an earlier claim. Indeed, we perceive such a result as capricious in effectively forcing a claimant company to delay its claim until it was absolutely certain about satisfaction of the test.

104. If that is correct, we see no reason in principle why the first claim should have to be withdrawn before a second claim is made. If there is a dispute with HMRC about whether the no possibilities test is fulfilled at the time of the first claim, we see no reason in principle why a claimant company should not make a later, protective, claim to preserve its position whilst the dispute is resolved. The claimant company should not be forced to abandon its first claim because, if it is a valid claim, it will have timing advantages over a later claim in terms of the time for set-off against total profits and thus for payment of corporation tax. But nor should it be faced with having to postpone a clearly valid claim, made when the test had clearly become fulfilled, until the first claim had been resolved.

105. Accordingly, in our view, sections 402 and 403 permit a great deal of flexibility. Schedule 18 lays down rules for the making of a claim which are detailed and appear more prescriptive. In the domestic self-assessment context they are, as we have described, pragmatic and flexible. The difficulty arises when trying to apply their prescriptive terms to a situation for which they were not designed, namely where the surrendering company is a foreign company and the losses can be surrendered only once the no possibilities test is satisfied. The question for us, still dealing with the general level, is the extent to which those provisions ought to be moulded to give effect to the Community rights which exist in that situation.

106. As to paragraph 67, there is clearly no need for any moulding. Paragraphs 68 and 69 need to be taken together.

107. As we see it, paragraph 69(2) makes no sense, if applied literally, in the context of a claim for group relief in respect of a foreign surrendering company. The "amount available for surrender" in paragraph 69(2) is not well defined in the context of the no possibilities test by reference to the definition in paragraph 69(3). In relation to a UK surrendering company, the tax return will reveal all the relevant information for ascertaining the amounts falling within section 403(1). But for the foreign surrendering company, that is not so. First of all, there is no UK tax return. Secondly, even if reference to the tax return can be read as a reference to the equivalent document in the Member State of residence of the surrendering company, that document will only provide information relevant to ascertaining the loss according to local tax law not UK tax law and will not reveal the information relevant to determining what, if any, part of those losses satisfied the no possibilities test.

108. There are then (at least) two approaches to the necessary disapplication or moulding:

> (1) First, paragraph 69(2) should simply be ignored. The claimant company then makes its claim, for the purposes of section 402, for group relief based on its view of the amount which falls within the no possibilities test. Provided that that claim has been made within the time limit in paragraph 74, the claim is one which must be accepted or challenged by HMRC. The challenge – for instance on the basis that the no possibilities test was not satisfied in relation to the whole or some part

> of the losses claimed – must then be adjudicated on by the Tax Tribunal. To the extent that the losses claimed exceed the losses which are ultimately shown to be available for surrender (that is, which satisfy the no possibilities test), relief is to be refused but the claim remains valid, and is to be allowed, for those losses satisfying the test.
>
> (2) Secondly, "the amount available for surrender" is to be read as a reference to the amount which is <u>in fact</u> available for surrender applying the no possibilities test at the time the claim is made. As in the first alternative, a dispute about the amount will be adjudicated upon by the Tax Tribunal. But if the amount of losses which satisfy the no possibilities test turns out to be less than the amount claimed, the whole claim fails as ineffective under paragraph 69(2). This is especially so if the no possibilities test is not satisfied at all because then there is no amount at all to which the procedurally valid claim applies and which can be said to be a "claim" within section 402.

If the first of these approaches is adopted, the fact that the first claim has been made does not preclude the making of the second claim, even where the first claim is not withdrawn. For reasons already given, we do not consider that sections 402 and 403 themselves prohibit such a course. Further, there is nothing in Schedule 18 either which produces that result. It cannot, we think, be said that the Second Step of paragraph 69(3) produces that result because, on the hypothesis under consideration on the first alternative, paragraph 69 does not apply. It is not possible to "cherry pick" the Second Step in ascertaining the amount for which a second claim can be made.

109. If this first approach is adopted, there is no reason to disapply or remould paragraph 68. We do not think that the principle of effectiveness would be compromised by a need for the requirements of paragraph 68 to be observed. It is not unreasonable to expect a claimant to specify the amount of the relief claimed. The fact that the claim is made in an excessive amount does not matter because the claim will, following agreement with HMRC or an appeal to the Tax Tribunal, be quantified in its proper amount. Because paragraph 69 does not apply, the claim is not rendered ineffective.

110. In contrast, if the second approach to paragraph 69 is adopted, and if the requirements of paragraph 68 also have to be observed, the claimant is faced with the risk that its claim may turn out to be excessive with the result that it is invalid. It is true that a second claim could be made specifying a smaller amount but, by the time it is established that the first claim is excessive, it may be too late to make another claim. We consider that this would infringe the principle of effectiveness. It is certainly much more difficult for a valid claim to be made in respect of the losses of a foreign group company that in respect of a UK group company. We consider that it would be excessively difficult and thus an infringement of the principle. Paragraph 68 would thus need to be remoulded so that a claim could be made without specifying the precise amount claimed or, if an amount were specified, the claim could be qualified by words such as "or such lesser amount in respect of which the claimant is entitled to claim relief". Paragraph 69(2) would not then render the claim ineffective.

111. This latter approach to the inter-relationship between paragraph 68 and paragraph 69 is somewhat artificial. We are of the view that the appropriate moulding is to disapply paragraph 69 altogether but leaving the requirements of paragraph 68 to have full force.

112. To summarise: in our view, a claimant company seeking group relief in respect of the losses of a foreign group company can make successive claims, provided that all those claims are made within the time limit for claims specified by paragraph 74. It does not have to withdraw an earlier claim before making another claim. The validity of the later claim depends on the facts as they are at the time of the later claim. If the first claim results in no relief being given because at the time that first claim is made the no possibilities test is not fulfilled in respect of any part of the losses in respect of which relief is claimed, a later claim can be made for such amount of those losses as satisfies the no possibilities test as at the time of the later claim. If an earlier claim is valid in respect of part of the losses (because the no possibilities test is satisfied in respect of part) then a later claim can be made for the balance. This, in our view puts the company claiming group relief for the losses of a foreign group company in effectively the same position as though it were claiming such relief for domestic losses, after taking account of those factors and difficulties which are not present in the domestic context. It does not put the claimant company in any better a position (save possibly – and if so, legitimately – in relation to cash flow) than if it waits until the last possible moment within the time limit period to make its claim, that is, the point at which it is most likely to be able to satisfy the no possibilities test.

113. We also add that this is consistent with the decision in the Court of Appeal: at [41] Chadwick LJ stresses that differential treatment as between the way losses of resident and non-resident companies are claimed should be avoided. He points out that in the case of losses of a resident company a claim can be made up to the time when the period for making claims ends, and that this should be so for claims for losses of a non-resident company, so that the decision to claim the losses can be made on the basis of the facts as they are at the end of the period within which the claimant company is permitted to make its claim.

The specific level of M&S – self-assessment years

114. These conclusions reduce the scope of issues concerning special transitional provisions for M&S. In relation to the self-assessment years it follows from our analysis of the group relief and group relief claim provisions as they generally should be applied to give effect to the Community law right to claim losses of a foreign group company where those losses satisfy the no possibilities test that all the claims sequentially made by M&S are valid and should be given effect to. If it transpires that at the time a claim was made there were no losses which satisfied the no possibilities test, such a claim has no effect, but does not, as HMRC have argued, result in a later claim being invalid. If it transpires that at the time a claim was made there were fewer losses which satisfied the no possibilities test than claimed, then, on the approach which disapplies paragraph 69 (the approach we favour) that claim has effect in relation to those losses which are eligible and a later claim holds good for the balance if as at the time of the later claim that balance then satisfies the no possibilities test. If we are wrong in adopting that

approach so that paragraph 69 applies without any relaxation of the requirements of paragraph 68, then the claim is ineffective and, clearly a subsequent claim can be made whether or not the earlier claim is withdrawn.

115. In relation to M&S we would add only that it framed its group relief claims with care and circumspection in response, no doubt, to the developing situation in relation to MSG and MSB as those companies moved to dissolution and to their understanding of the law as they understood it from the law as it was declared over the sequence of litigation. There is nothing in the terms of the actual group relief claims made by M&S which leads us to apply our conclusions at the general level in a way which results in those claims being disregarded or invalid by reason of their own specific terms: on the contrary, those terms seem well-tailored to apply in the specific circumstances of the M&S group, the group relief claims provisions, and the particular features and difficulties which arise in claiming relief for the losses of a foreign group company, and to allow M&S to exercise such Community law rights as it has in that regard.

116. If we are wrong in what we have said about the general level, we need to consider whether M&S in its particular circumstances can nevertheless claim that effect should be given to its Community law rights. This is a question which is rather more clearly raised in relation to the group relief claims it made in relation to losses arising in the pay and file years.

The group relief claims for the pay and file years

117. As mentioned, M&S made group relief claims in respect of losses of MSG for the years ended 31 March 1996, 1997, 1998 and 1999 and in respect of losses of MSB for the years ended 31 March 1998 and 1999. In relation to those claims the relevant provisions are sections 402 and 403 ICTA1988, and (in respect of the procedure for making claims) Schedule 17A ICTA1988.

118. For the losses of MSG for the years 1996 and 1997 the first group relief claim was made on 20 March 2007, and a further, alternative, claim was made on 12 December 2007. For the losses of MSG for the year 1998 the first group relief claim was made on 31 March 2000, and for the year 1999 on 30 March 2001, with, in each case, alternative claims submitted on 20 March 2007 and 12 December 2007.

119. For the losses of MSB for the years 1998 and 1999 the first group relief claims were made on 27 June 2007 with, in each case, alternative claims submitted on 12 December 2007 and 11 June 2008.

120. The short point to note is that the pay and file regime has a more restrictive scheme than the self-assessment regime as to the time limits in which a claim must be made, and only the first group relief claims made in respect of the MSG losses for 1998 and 1999 were within those time limits. Under Schedule 17A HMRC have a power to extend those time limits, but (as yet) have refrained from exercising that power to admit the later, alternative, group relief claims made by M&S. At the time the first group relief claims were made (31 March 2000 and 30

March 2001 respectively) MSG was still trading and so M&S cannot show that at that time there was no possibility that the losses would be used locally.

121. In examining the pay and file years, as with the self-assessment years, it is necessary to see first whether (and if so, the extent to which) the relevant provisions need moulding to give effect to a claimant company's Community law rights to claim group relief for the losses of a foreign group company.

122. In relation to sections 402 and 403 ICTA 1988, the position is the same as it is for the self-assessment years since in all material respects the provisions are the same for both regimes. Our conclusions are that a degree of moulding is required to deal with the particular features of the Community law right to claim losses of a foreign group company, and that there is nothing inherent in those sections themselves which precludes a sequence of group relief claims as circumstances change with regard to the outcome of the no possibility test (see paragraphs 98 to 104 above).

123. Schedule 17A does differ from its self-assessment counterpart. Paragraph 6 provides that a group relief claim is to be made by being included in the corporation tax return for the period for which the claim is made, or an amendment to that return. As with self-assessment, the surrendering company must consent to the surrender for a claim to be valid, and notice of consent must include the amount of relief being surrendered; the surrendering company must make a corporation tax return (or amend its return) to take account of the surrender (paragraph 10). A group relief claim may be made for less than the full amount of losses available (paragraph 7), but it must be for an amount which is quantified at the time the claim is made (paragraph 8). If a corporation tax return has resulted in an assessment which is being appealed, a group relief claim can be made which, as to the amount claimed, is conditional upon the outcome of the matter under appeal (paragraph 9).

124. It is to be noted that there is no provision in Schedule 17A equivalent to that of paragraph 69(2) of Schedule 18 FA 1998 ("A claim is ineffective if the amount claimed exceeds the amount available for surrender at the time the claim is made"). Paragraph 8 of Schedule 17A, which requires that a claim is to be for an amount which is quantified at the time the claim is made, corresponds directly to paragraph 68(1) of Schedule 18, and, for the reasons we have stated in relation to paragraph 68(1), no moulding of paragraph 8 of Schedule 17A is required to permit claims for losses of a foreign group company.

125. We conclude, therefore, at what we have described as the general level, that the position in respect of group relief claims for losses of a foreign group company under the pay and file regime is similar to that under the self-assessment regime. In particular, if such a group relief claim is made and as at the time it is made there are no losses eligible to be surrendered because the no possibilities test is not satisfied, in order to give effect to Community law rights a subsequent group relief claim can be made (provided it is made within the Schedule 17A time limits for making claims) and if as at that later time there are losses which are eligible to be surrendered, the claim will be compliant with the Schedule 17A requirements as they are to be applied in such a case.

The M&S level – whether M&S specially has effective Community law rights

126. It is necessary to consider whether, having regard to its particular circumstances, M&S should be treated as having effective Community law rights notwithstanding that domestic provisions, even when moulded to allow the exercise of Community law rights at the general level, prevent the exercise of such rights. This question arises most clearly in relation to the out of time group relief claims for the pay and file years, but M&S argues that, more generally, as the taxpayer which has led the way in establishing these particular Community law rights (and in doing so has had to tread uncharted paths) it should not be prejudiced if it has, through ignorance of what the courts might ultimately determine, failed to comply with the procedural requirements found to be necessary in asserting its Community law rights in a manner which is compliant with domestic legislation.

127. We will deal first with the out of time group relief claims for the pay and file years.

128. As mentioned, in relation to the losses of MSG for 1998 and 1999, the first group relief claims for those years were in time but when made the no possibilities test was not satisfied. The subsequent group relief claims for those years, and the first and all subsequent group relief claims for losses for all other years subject to pay and file (both for MSG and MSB) were made outside the time limits provided for by Schedule 17A ICTA 1988. Mr Ewart says that M&S's claims ought to have been dismissed. The Tribunal decided otherwise. They concluded that the principle of effectiveness (which we have mentioned and to which we said we would return) required that the domestic time limit for making a group relief claim should be disapplied. They considered that M&S should be entitled to make a new claim for group relief within a reasonable time after the ECJ Judgment in place of the first group relief claim which the Tribunal had decided was invalid. In reaching its conclusion, the Tribunal considered the (*obiter*) section of the judgment of Chadwick LJ in the Court of Appeal, at paragraphs 51*ff* from which one can see he was attracted by the conclusion which the Tribunal subsequently reached.

129. The Tribunal considered two lines of cases in the ECJ to which we will need to come in more detail in a moment. We simply note their descriptions at this stage. The first line is where a person has a Community law right but does not know it and fails to take the necessary action to assert it within a reasonable domestic law time limit. The principle of legal certainty, the Tribunal said, means that he loses the right.

130. The second line of cases applies where a person has a Community law right which he is in time to assert but, before he does so, it is taken away without any transitional provision. In such a case, the principle of effectiveness allows him to assert the right in spite of the domestic time limit.

131. The Tribunal considered that the present case was not on all fours with either line of cases. They noted that M&S had made a claim in order to assert what it

then considered was its Community law right within the reasonable time limit laid down by domestic law. The ECJ Judgment showed that M&S did have a right, but it was a narrower one than the one it had claimed. The original claim was therefore defective. The same claim made later would have succeeded but for the (reasonable) time-limit which, it was noted, HMRC had power to extend. The Tribunal considered that in those circumstances the ECJ would consider that the principle of effectiveness was breached because the right was rendered impossible or excessively difficult to exercise.

132. The Tribunal considered that the principle of legal certainty was weaker than in the first line of cases because in the present case a claim had actually been made within the domestic time limit. The State knows that the person has exercised the right and has done so in order to ascertain whether the right exists so that re-exercising the right will not come as a surprise – and all the more so where HMRC has a discretion to extend the time limit in any case. The Tribunal characterised this as a transitional case (and in that sense similar to the second line of cases) for M&S which raised the issue of whether it had a special right. Other persons would come within the first line of cases, not having made any claim at all, and thus lose the right by failing to assert it.

133. There is, we perceive, a slight irony in that last observation of the Tribunal. Before us, in the context of a different argument concerning the withdrawal of earlier claims for self-assessment years, M&S argue that they are in fact worse off than other persons because others can make an original claim within time but knowing of the need to fulfil the no possibilities test at the time they make such claim, whereas M&S is being met with what it describes as opportunistic technical points to defeat its claims.

134. The Tribunal took its steer very much from Chadwick LJ’s hint (as they described it) disagreeing with Mr Ewart’s suggestion that he had misunderstood the second line of cases. He must have realised that the present case was not the same as the second line of cases but, according to the Tribunal, he must have seen similarities in that they were both transitional problems caused by domestic legislation expressly providing that the Community right could not be exercised at the appropriate time.

135. In order to see whether the Tribunal’s approach is open to challenge, we need to go back to the principle of effectiveness and to the two lines identified by the Tribunal. We take, as Mr Ewart has done, the decision of the ECJ is Case C-62/00 *Marks & Spencer plc* [2002] ECR I-6325 [2003] QB 886 (*Marks & Spencer I*”) as a starting point. As paragraph 35 of the judgment shows, the ECJ had previously held that, in the interests of legal certainty, which protects both the taxpayer and the administration, it is compatible with Community law to lay down reasonable time-limits for bringing proceedings (reference being made to Case C-228/96 *Aprile* [1998] ECR I-7141 (“*Aprile II”*)). Such time-limits (i.e. reasonable domestic time-limits) are not liable to render virtually impossible or excessively difficult the exercise of the rights conferred by Community law.

136. It is clear that reasonable time-limits are compatible with Community law even if the consequence is that the claimant’s action is dismissed: see for instance Case C-90/94 *Haahr Petroleum Ltd* [1997] CR I-4085 at paragraph 48. Mr Ewart submits that it makes no difference to that proposition that the substantive Community law principles applicable to the claim might only have been clarified

by the ECJ after the expiry of the applicable time limit, referring to *Aprile II*. His submission in this regard finds recent support in the Court of Appeal decision in *F J Chalke Ltd and another v HMRC* [2010] EWCA Civ 313 (a decision handed down after the hearing of the present case) where it is confirmed that Community law rights may be lost where the claimant fails to exercise within applicable time limits those rights due to his ignorance of their existence or the development of the law by judicial decisions (see [55] and [69]).

137. *Aprile II* concerned a claim for repayment of charges unlawfully levied in respect of customs transactions and which Italian finance authorities had refused to repay. The charges were levied in November 1990 as is apparent from paragraph 7 of the Opinion of Advocate General Ruiz-Jarabo. The judgment in *Aprile II* explains, at paragraphs 6 and 7 as follows:

> "6. By judgment of 5 October 1995 in Case C-125/94 *Aprile v Amministrazione delle Finanze dello Stato* [1995] ECR I-2919 (hereinafter 'Aprile I'), the Court held, first, that Directive 83/643, as amended by Directive 87/53, was not applicable to customs formalities in respect of goods from non-member countries, and, second, that the Member States were not entitled unilaterally to impose charges having equivalent effect in trade with those countries.
>
> 7. Following the judgment in Aprile I, it fell to the national court to consider an objection raised by the defendant administration to the effect that Aprile's claimed right to reimbursement had become statute-barred by virtue of [the relevant Italian legislation]"

138. It can be seen that the charges were unlawfully levied in November 1990 but that the clarification of the applicable substantive law was only obtained in 1995 when the Court gave its decision on the preliminary reference. This was after expiry of the Italian time limit, which was 3 years. Italy was permitted to rely on that time limit provided that it applied in the same way to actions based on Community law for repayment of such charges as to those based on national law. Further, it was held that Community law does not prohibit a Member State from resisting actions for repayment of charges levied in breach of Community law by relying on a time-limit under national law even if that Member State had not yet amended its national rules in order to render them compatible with those provisions.

139. It does not follow from *Aprile II* that national time-limits can always be relied on even where the time limit is *prima facie* of a reasonable length. They cannot be relied on, for instance, where national legislation has effect in relation to an existing accrued Community right, for example where the Member State shortens a limitation period with retroactive effect without providing an adequate transitional period. The reduced limitation period may be perfectly reasonable and in accordance with the principle of effectiveness once it has been in force for a period of time. But that does not prevent the new shorter time-limit infringing the principle of effectiveness in relation to persons whose existing rights are being curtailed by its introduction – although in such a case it might be said that it is not the shorter-time limit itself which infringes the principle of effectiveness, but its imposition without reasonable transitional protection for those whose accrued rights are otherwise curtailed. The applicable principles are summarised in paragraphs 36 to 42 of the judgment of the ECJ in *Marks & Spencer I*.

"36 Moreover, it is clear from the judgments in *Aprile* (paragraph 28) and *Dilexport* (paragraphs 41 and 42) that national legislation curtailing the period within which recovery may be sought of sums charged in breach of Community law is, subject to certain conditions, compatible with Community law. First, it must not be intended specifically to limit the consequences of a judgment of the Court to the effect that national legislation concerning a specific tax is incompatible with Community law. Secondly, the time set for its application must be sufficient to ensure that the right to repayment is effective. In that connection, the Court has held that legislation which is not in fact retrospective in scope complies with that condition.

37 It is plain, however, that that condition is not satisfied by national legislation such as that at issue in the main proceedings which reduces from six to three years the period within which repayment may be sought of VAT wrongly paid, by providing that the new time-limit is to apply immediately to all claims made after the date of enactment of that legislation and to claims made between that date and an earlier date, being that of the entry into force of the legislation, as well as to claims for repayment made before the date of entry into force which are still pending on that date.

38 Whilst national legislation reducing the period within which repayment of sums collected in breach of Community law may be sought is not incompatible with the principle of effectiveness, it is subject to the condition not only that the new limitation period is reasonable but also that the new legislation includes transitional arrangements allowing an adequate period after the enactment of the legislation for lodging the claims for repayment which persons were entitled to submit under the original legislation. Such transitional arrangements are necessary where the immediate application to those claims of a limitation period shorter than that which was previously in force would have the effect of retroactively depriving some individuals of their right to repayment, or of allowing them too short a period for asserting that right.

39 In that connection it should be noted that Member States are required as a matter of principle to repay taxes collected in breach of Community law (Joined Cases C-192/95 to C-218/95 *Comateb and Others* [1997] ECR I-165, paragraph 20, and *Dilexport*, paragraph 23), and whilst the Court has acknowledged that, by way of exception to that principle, fixing a reasonable period for claiming repayment is compatible with Community law, that is in the interests of legal certainty, as was noted in paragraph 35 hereof. However, in order to serve their purpose of ensuring legal certainty limitation periods must be fixed in advance (Case 41/69 *ACF Chemiefarma v Commission* [1970] ECR 661, paragraph 19).

40 Accordingly, legislation such as that at issue in the main proceedings, the retroactive effect of which deprives individuals of any possibility of exercising a right which they previously enjoyed with regard to repayment of VAT collected in breach of provisions of the Sixth Directive with direct effect must be held to be incompatible with the principle of effectiveness.

41 That applies notwithstanding the argument of the United Kingdom Government to the effect that the enactment of the legislation at issue in the main proceedings was motivated by the legitimate purpose of striking a due balance between the individual and the collective interest and of enabling the

State to plan income and expenditure without the disruption caused by major unforeseen liabilities.

42 Whilst such a purpose may serve to justify fixing reasonable limitation periods for bringing claims, as was noted in paragraph 35, it cannot permit them to be so applied that rights conferred on individuals by Community law are no longer safeguarded."

140. It is clear from those paragraphs that it was the retrospective curtailment of an existing right which led to the conclusion that the UK legislation was ineffective to impose the new time limit on these transitional cases. Limitation periods must be fixed in advance if they are to serve their purpose of ensuring legal certainty.

141. It was this aspect of the principle of effectiveness with which the House of Lords was concerned in *Fleming (t/a Bodycraft) v HMRC* and *Condé Nast Publications Ltd v HMRC* [2008] UKHL 2, [2008] 1 WLR 195. The cases were all about the retrospective imposition of time limits and the need for transitional arrangements in relation to those new limits in order to comply with the principle of effectiveness. The House of Lords said nothing about the decision in *Aprile II* or *Haarh Petroleum Ltd* and did not address the question with which we are now concerned. Nor did the Court of Appeal do so in either *Fleming* [2006] EWCA Civ 70 or *Condé Nast* [2006] EWCA Civ 976.

142. The Tribunal set out Lord Neuberger's exposition, in *Fleming* and *Condé Nast*, of the propositions which he derived from his analysis of the European jurisprudence: we do not think it necessary to set it out again since it is mainly about the introduction of retrospective legislation. They then distinguished *Aprile II* and *Haarh Petroleum Ltd* as we have already explained, relying on the "hint" given by Chadwick LJ in the present case.

143. We do not find it entirely surprising that Chadwick LJ gave the hint which he did. When hearing *Condé Nast* in the Court of Appeal, he was dealing with an argument very much focused on the operation of the principle of effectiveness in the context of the introduction of a retrospective time limit. He did not need to consider, and he certainly did not in fact address, the application of the principle of effectiveness in situations where the ECJ had already held such time limits to be valid in accordance with considerations of legal certainty. *Aprile II* and *Haarh Petroleum* were not, so far as we can see, cited. Without the benefit of citation of those cases, it is not difficult to see that, with *Condé Nast* reasonably fresh in his mind, Chadwick LJ would have perceived an analogy with the present case. The point appears to have arisen at a late stage. It did not arise for decision and Chadwick LJ's comments did not, clearly, form part of his decision. Even he only went so far as to say that the decision of the Court of Appeal provided "support" for the conclusion. We must form our own view in the light of the full argument and citation which we have received.

144. As mentioned, M&S makes a further point, which commended itself to the Tribunal: M&S says that, according to the ECJ jurisprudence, a time limit imposed by national law which curtails the exercise of Community law rights is justifiable on the principle that there must be legal certainty. If legal certainty is not an issue, then the principle of effectiveness should prevail to allow a person affected by a time limit to exercise his Community law rights. M&S argue that since HMRC were aware that M&S was making group relief claims (some of

which were in time) and was thereby seeking to protect its rights, certainty or finality was no longer an issue. This is a situation, argue M&S, which is different from that where a litigant fails within a time limit to make a claim to protect its rights because it was not aware that it could make such a claim, and where it is reasonable that legal certainty should prevail. In this regard M&S rely upon certain passages in the judgment of the ECJ in Case C-312/93 *Peterbroeck* at §20 and observations in paragraph 69 of the Opinion of Advocate General Jacobs in Case C-188/95 *FantaskA/S and Others v Industriministeriet (Erhvervsministeriet)*.

145. Miss Shaw referred to paragraph 14 of the judgment in the *Peterbroeck* case, which is as follows:

> **"**14. For the purposes of applying those principles, each case which raises the question whether a national procedural provision renders application of Community law impossible or excessively difficult must be analysed by reference to the role of that provision in the procedure, its progress and its special features, viewed as a whole, before the various national instances. In the light of that analysis the basic principles of the domestic judicial system, such as protection of the rights of the defence, the principle of legal certainty and the proper conduct of procedure, must, where appropriate, be taken into consideration."

Miss Shaw argues that the time limit for making claims imposed by the group relief provisions is a procedural provision whose purpose is the procedural one of alerting HMRC that a claim has been made, and as such, if it renders impossible the exercise of the Community law right to claim group relief for foreign losses, it should not be sustained on the grounds that to do so is required to give effect to the principle of legal certainty where legal certainty is not a justification for a time limit of this kind.

146. Miss Shaw also relies on the judgment of the ECJ in Case C-327/00 *Santex SpA* [2004] 2 CMLR 30. This case concerned procurement notices for public supply contracts and the question was whether the imposition of time limits which purported to rule out any challenge to the validity of those notices could be relied upon by the national authority. In principle, a time limit was valid and the 60 day limit in fact applying appeared reasonable. But this result is to be qualified by what was said by the ECJ at paragraphs 56 to 58 of the judgment:

> "56. However, for the purpose of applying the principle of effectiveness, each case which raises the question whether a national procedural provision renders application of Community law impossible or excessively difficult must be analysed by reference, in particular, to the role of that provision in the procedure, its progress and its special features, viewed as a whole [reference being made to *Peterbroeck*].
>
> 57 Consequently, although a limitation period such as that at issue in the main proceedings is not in itself contrary to the principle of effectiveness, the possibility that, in the context of the particular circumstances of the case before the referring court, the application of that time-limit may entail a breach of that principle cannot be excluded.
>
> 58 From that point of view, it is necessary to take into consideration the circumstance that, in this particular case, although the disputed clause was

brought to the notice of the parties concerned at the time of the publication of the notice of invitation to tender, the contracting authority created, by its conduct, a state of uncertainty as to the interpretation to be given to that clause and that that uncertainty was removed only by the adoption of the exclusion decision."

147. In our view the Tribunal were wrong to hold that the time limits for making a group relief claim should be set aside to allow M&S to make a claim after it became aware that such a claim, to be effective, must satisfy the no possibilities test. That seems to us to be an extension of the application of the principle of effectiveness which cannot be justified by the ECJ jurisprudence. The ECJ has consistently upheld the right of a Member State to impose time limits within which a claimant must make his claim, provided that the time limit is reasonable, and provided that, if a time limit is reduced, accrued rights are protected by reasonable transitional arrangements. The right to impose and enforce time limits is a means by which the Community law principle of legal certainty is given effect to. The cases show that the principle of legal certainty prevails, notwithstanding that in consequence it is made impossible for a claimant to enforce a Community law right which he could otherwise assert. In that sense the principle of legal certainty prevails over the principle of effectiveness.

148. Accordingly, where the no possibilities test is satisfied for the first time only after the expiry of the relevant time for making a claim, the principle of effectiveness does not require that the domestic legislation should be moulded to allow a claim to be made however far in the future the no possibilities test might first become satisfied.

149. The cases also show that this is so even where the claimant was not aware of his Community law right (and therefore made no claim to assert that right) until after the time limit had expired. In such a case the principle of effectiveness does not come into play: it is not the existence of the time limit which makes it impossible or excessively difficult for the claimant to exercise his Community law right, but his ignorance of the existence of that right. This is consistent with the cases where there is a reduction in the time limit curtailing accrued rights without adequate transitional provision: it is the curtailing of the rights which makes it impossible for the claimant to assert his rights, not the time limit (even the reduced time limit) as such.

150. That being so, it is not material that M&S made some sort of claim (but one which failed to meet the requirements for an effective claim as subsequently declared by the courts) within the time limit. It is not material that this signalled in some way to HMRC that it would assert its rights as and when it had discovered how to do so (or, more correctly, as and when it had discovered what action it needed to take – be it liquidation of MSG and MSB, or whatever – it order to be in a position to do so). It remains the case that the existence of the time limit has not made it impossible for M&S to assert its right (indeed, M&S did make a claim within the time limit, but it was ineffective); nor has there been any change in law (such as a reduction in the time limit) which has made it impossible for M&S to assert its right: it was M&S's ignorance of the action it needed to take to put it in the position to make a claim which complied with the requirements of a valid

claim which caused it to be in the position where it could not have the benefit of its Community law rights.

151. It does not seem to us, as it appeared to the Tribunal, that the principle of legal certainty is qualified (or, as the Tribunal put it, the case for applying it is weaker) in a case where some unsuccessful attempt has been made within a time limit to assert the right in question. We see nothing in case law to suggest that, nor do we see any basis for that view. The purpose of any limitation period is to provide certainty and finality: a claim can be pursued if it is made within that period, but not otherwise. If for any reason a claim made within that period proves to be defective and cannot successfully be pursued, it is not open for the claimant to make a further claim on a different basis (far less a further claim by reference to changed circumstances), arguing that the other party is not prejudiced because it was put on notice that, eventually, a successful claim was likely to ensue. Such an approach would render nugatory the legal certainty which is the sole purpose of the limitation period.

152. The Tribunal also justified its approach on the basis that M&S was in a special, transitional, position, which brought its case more within the ambit of the line of authorities concerned with transitional arrangements in the case of accrued rights curtailed by the reduction of a time limit. That, too, seems to us to be an extension of existing authority which cannot be supported. The courts have been concerned to allow effective transitional arrangements, by way of applying the principle of effectiveness, only where the State has taken action (reducing time limits) which has rendered it impossible for a claimant to exercise rights which, absent such action, he could have enforced. That is far removed from the circumstances of M&S in the present case. M&S had a right (to claim group relief for the losses of a foreign group company) which, if it could have shown the claim satisfied the required conditions, it could have exercised at any time until the time limit expired. There was no action on the part of HMRC or the UK government to extinguish that right or otherwise make it impossible for M&S to assert that right. In these circumstances it seems to us that the case cannot be sustained that M&S's position should, by analogy, be aligned with that of those whose rights have been curtailed.

153. We do not accept Miss Shaw's argument that the time limit for making group relief claims should be viewed only as some procedural matter undeserving of being justified or buttressed by the principle of legal certainty. The tax system is littered with time limits within which either the taxpayer or HMRC must take action of some sort or another, including (in the case of the taxpayer) making claims for relief. Those time limits are there to ensure the orderly and timely conduct of affairs and consistency in treatment between taxpayers, an important part of which is to provide certainty and finality, as with any limitation period. This is so even where (as is the case in relation to claims made for the pay and file years) HMRC have a discretion to allow out of time claims.

154. We do not think that the case of *Peterbroeck* assists in this regard, since it is a case concerned not so much with time limits, but rather with matters of procedure to do with the ability of a national court to entertain a matter of Community law of its own motion, and the significance of any general observations in that case must be weighed against the explicit judgments of the ECJ upholding the rights of states to rely on reasonable time limits. We do not think that the case of *Santex*

SpA assists M&S either. The decision turned very much on the particular facts of the case: the public authority had by its conduct created a state of uncertainty (i.e. about the true meaning of the disputed clause) and it was only once it had made the exclusion decision (i.e. the decision to exclude the applicant from the tendering process) that the uncertainty was removed, by which time it was too late for the applicant to challenge the notice of invitation to tender. Thus it was held that

> "the changing conduct of the contracting authority might be considered, in view of the limitation period, to have rendered excessively difficult the exercise by the harmed tenderer of the rights conferred on him by Community law."

155. We do not detect any parallel to that approach applicable in the present case.

156. The second area which needs to be addressed at the specific level of M&S is this. It is said that it was not until the ECJ Judgment that M&S could have anticipated that a test such as the no possibilities test would be introduced into the jurisprudence. Accordingly, M&S should not only be given time after the decision to make its claim, it should be given time to put itself into a position where it could make an effective claim. Thus it is said that the clearest way of satisfying the no possibilities test would have been to put each company into liquidation and to have it dissolved. M&S should, it is said, be allowed a transitional period within which to effect that course of action.

157. We disagree with that argument. The principle of effectiveness is concerned with giving effect to Community rights. It is concerned with ensuring that such rights as a person has under Community law are recognised and given effect to in a Member State which has not properly reflected such rights in its own domestic law. It is no part of that principle that a person should be given the opportunity to bring about a new state of affairs giving rise to the existence of new rights which he does not already have, in order to enforce them under Community law when they would be unenforceable under domestic law.

158. In any event, for the pay and file years, the no possibilities test was not satisfied, as is apparent from the Substantive Decision, until the commencement of the liquidations of MSB and MSG in October 2006, by which time it was too late, if domestic time limits applied, for M&S to make its claims for group relief. M&S could not, even if it had known the law, have made valid claims within the time limit because the no possibilities test was not fulfilled. In those circumstances, the principle of effectiveness cannot be invoked since there was no right under Community law in respect of which a claim could be made within the time limit; and for reasons given in the immediately preceding paragraph, it is not part of the principle of effectiveness that a company must be given an opportunity to create a new situation so as to allow it to assert a right which it would not otherwise have.

Wrong at the general level

159. Suppose we are wrong at the general level and that HMRC is correct in saying not only that paragraph 69 does not apply at all but also that a new claim cannot be made until an earlier claim is withdrawn. The question would then arise whether the principle of effectiveness was infringed. We prefer not to express a final view on that. But assuming that it is not infringed at the general level, the question remains whether M&S is entitled to a transitional period during which, contrary to the general rule, it is to be entitled to make a claim without

withdrawing its earlier claims. It would want to do so because HMRC will not concede that, if the earlier claims are withdrawn, a valid later claim can be made. Thus M&S's position would compare adversely to that of another company which had not made a claim at all but now sought to do so within any relevant time limit.

160. We cannot see that there is a basis for M&S to be entitled to special treatment in these circumstances. As we have held in relation to the question of time limits for the group relief claims made in the pay and file years, the circumstances of M&S were not such that it was rendered impossible, or excessively difficult, for M&S to exercise its rights to make a valid claim. It could have made a valid claim (or could have taken the required action to put itself in a position to make a valid claim) if it had had a correct understanding of the law as it was eventually declared by the courts. The decisions of the courts did not confer further rights on M&S or change the rights it had – they explained those rights as they had always existed. If, therefore, the moulding of the group relief claim provisions necessary to give effect to Community law rights does not assist M&S in relation to the claims it has actually made, we cannot see a legal principle which comes to the aid of M&S in its particular circumstances.

The application of the no possibilities test

161. We have to consider next the application of the no possibilities test to the circumstances of M&S and the losses of MSG and MSB and the group relief claims made by M&S in relation to those losses.

162. We have set out earlier in this decision the ECJ Judgment as it explained the no possibilities test, and the further exposition of that test in the UK context of group relief claims in the decisions of Park J and the Court of Appeal. The Tribunal summarised the position as it appears from those various decisions at paragraph 16 of its decision, and before us both parties accepted that as an accurate and helpful summary. It may be of assistance to set it out here:

> "16. Therefore we must consider 'recognised possibilities legally available given the objective facts of the company's situation at the relevant time.' This is different from there being 'little or no real likelihood, or that the claimant (or the surrendering company) had no intention, that losses could or would be set against future profits.' It is also the case that '"no possibility" in the second condition is to be read as "no real possibility"; in the sense that a real possibility is one which cannot be dismissed as fanciful.' The second condition must also have regard to 'the objective facts of the company's situation at the relevant time.' Park J's example in [38] shows that the fact that the loss company had ceased to trade was not enough if the losses could still be carried forward (and the fact that the company had no intention of receiving further income was also irrelevant)."

163. The Tribunal heard extensive evidence as to the circumstances of MSG and MSB at the different times the various group relief claims were made, and expert evidence as to the tax rules in the relevant jurisdictions relating to the utilisation of losses and also as to the scope of the actions which the two respective companies could take once liquidation proceedings had been commenced.

164. The Tribunal's decisions on the application of the no possibilities test can be summarised as follows:

(1) The no possibilities test is to be applied to each euro of losses, so that the fact that some losses were utilised in the liquidation period did not preclude a finding that there was no possibility of utilising the balance of the losses;

(2) At any time up to the date on which liquidation of the respective companies commenced there was a possibility that the losses could be utilised, and so at the time when any group relief claims were made during the period up to that date (in effect, at the time the first group relief claims were made) the no possibilities test was not satisfied, and the claim failed. Should HMRC eventually succeed in its argument that the proper time to apply the test is at the end of the accounting period in which the losses accrue (rather than when the group relief claim is made) it follows that the test would not be satisfied, since all the losses in question accrued in accounting periods ending before liquidation commenced;

(3) Once liquidation had commenced there was no real possibility that the losses could be utilised except to the limited extent of setting them against investment and similar income arising in the course of realising and distributing assets in the liquidation process. Accordingly, at the time of the second and each of the subsequent group relief claims the no possibilities test was satisfied to the extent that losses could not be utilised against income arising in the normal course of the liquidation process.

165. For the reasons already give (see paragraphs 46 and 47 above) we agree with the Tribunal that the correct approach is to look at each euro of loss. Mr Ewart objected to this approach in that it introduces a balance of probabilities test to ascertain the amount of euros which do and do not satisfy the no possibilities test which he saw, perhaps not unreasonably, as something of a logical inconsistency in applying a test as uncompromising as a “no possibilities” test. But the test as laid down in the ECJ Judgment has to be applied in the real world – a factor which is self-evident and is implicit in the Court of Appeal’s formulation that it is a “no real possibility” test, and Park J’s assertion that it is necessary to have regard to the possibilities legally available ”given the objective facts of the company’s situation at the relevant time”. In that context, if there is in any accounting period a tranche of losses in respect of which a claimant can show that there is no real possibility that they will be utilised, the justifications identified by the ECJ for not giving relief for foreign losses no longer hold good for those losses, and a claim should be allowed.

166. Mr Ewart’s first objection to the Tribunal’s conclusions in applying the no possibilities test was stated in these terms (taking the position of MSG as an illustration): losses were made in each of the years 1996 to 2001, but thereafter (as it happens, after trading ceased, but that is not material) MSG made profits. At the time of the second group relief claim (March 2007), if one is claiming relief for the losses of 2001 they must fail the no possibilities test because there was the possibility that they could be utilised against the profits of the succeeding years (and some losses – whether from 2001 or earlier years, it cannot be said which unless there is some rule of German tax law which is specific on the point – were in fact so utilised). The Tribunal, in attempting to apply the decision of the Court of Appeal that the no possibilities test must be applied at the time the group relief claim was made had, first of all, simply looked at the losses extant at that date (March 2007) and had asked whether, looking forward from that date those losses

could possibly be utilised and secondly, in order to determine the amount of losses which could be claimed for each year (recognising that some losses had in fact been utilised in years 2002 onwards) had been forced to devise and apply a system for notionally setting losses against subsequent profits (it chose "first in, first out", i.e. utilising losses first of the earliest year).

167. Mr Ewart's second (and more straightforward point) was that even if one adopted the Tribunal's approach it could not be said that there was no possibility that the losses as they stood at March 2007 – or at any time until the companies had been dissolved – could be utilised: it was, for example, possible (even if unlikely) that the liquidation could be terminated and a new and profitable business started up in the companies and the losses set against such profits.

168. As to Mr Ewart's first point, we see the difficulty presented by a literal reading of the ECJ Judgment and of applying the Court of Appeal decision, and we have analysed the possible approaches and set out our conclusions in paragraphs 48 to 55 above. For the reasons given there, and taking account of our decision also that the no possibilities test is to be applied on a euro by euro basis, we are of the view that the no possibilities test has to be applied at the time of the group relief claim (say, March 2007) and by reference to the losses that at that time remain unutilised. Mr Ewart's approach is tantamount to an argument that the no possibilities test is to be applied as at the end of the accounting period in which the losses claimed arise, and that argument has been rejected by the Court of Appeal. We accept that the approach which applies the no possibilities test to the losses for any year as they stand at the time of the group relief claim has to take account of what happens in the period from the end of the year until the time of the claim if losses are in fact utilised during that period so as to determine the extent (if any) to which the losses of a particular year are treated as utilised. As stated, the Tribunal applied a "first in, first out" method of utilising losses, and that seems to us to be both reasonable and pragmatic.

169. Before turning to Mr Ewart's second point we should deal with the position of M&S in relation to this issue. M&S's position is that if it is eventually decided that the only group relief claims it can rely on are the first group relief claims, then it wishes to argue that the Tribunal reached the wrong decision in holding that, since at the time those claims were made there was a real possibility that the losses as they then stood could be utilised at some future time, then as at that time the no possibilities test was not satisfied. We see no basis for challenging that decision of the Tribunal. The first claims were made on dates between 2000 and 2003 before either MSG or MSB was in liquidation, some being before, and some after, the company ceased trading. On the basis of the evidence the Tribunal concluded that, "there was nothing to prevent the losses being used by continuing to trade, or starting another trade or business. Whether or not this occurs is a matter of likelihood which is to be ignored." That, in our view, deals with the point correctly and entirely.

170. Mr Ewart considers that the Tribunal should have come to a similar conclusion when it applied the no possibilities test as at the time of the second and subsequent group relief claims, that is, notwithstanding that by then liquidation proceedings had been commenced in the case of both MSG and MSB.

171. The Tribunal heard expert evidence from both parties as to what action was possible in the course of the liquidation of the two companies. In the case of

MSG the evidence put forward by the expert called by M&S was that once a German company is in liquidation, the liquidator must confine himself to realising the assets and distributing the proceeds, and he cannot recommence the business or restart any new business. HMRC's expert said that the shareholder of a German company in liquidation could at any time halt the liquidation and re-launch the business activities of the company. The Tribunal accepted this as a qualification to the evidence given on behalf of M&S. As to MSB, HMRC's expert gave evidence to the effect that a Belgian company in liquidation only exists for the purpose of its liquidation, so that no new activities can be developed.

172. The Tribunal (having concluded that the no possibilities test is to be applied to each euro of losses), was concerned with that tranche of the losses which could not be utilised against investment or other income arising in the course of the liquidation proceedings. It concluded that once MSG was in liquidation there was no real possibility that the liquidation would be terminated and the business re-launched – any possibility of that occurring was fanciful. It followed that there was no real possibility that the tranche of losses could be utilised.

173. As we have said in the context of applying the no possibilities test on a euro by euro basis, the ECJ Judgment has to be applied in the real world. The Court of Appeal recognises this in drawing the distinction between a "real possibility" and a possibility which is "fanciful". The logic of HMRC's position is that the no possibilities test is satisfied only if there is some legal bar which prevents the losses being utilised in the future, as would be the case, for example, if the right to use them had time-expired under a provision of local law. That seems to us to be too restrictive, and if the ECJ had intended that to be their decision they would have made it plain. Rather, an element of judgment is required having regard to the circumstances.

174. Our conclusion as to the making of claims for the self-assessment years is that successive claims are valid to the extent that the no possibilities test is satisfied at the time of each claim, so that an earlier, ineffective, claim does not preclude a later claim for the same losses if at the time of that later claim the losses can then be claimed because the test is then satisfied. Applying this first to MSB, the fourth (and final) group relief claim in relation to losses arising in the self-assessment years was made after the company was dissolved, with the liquidator consenting to the surrender notwithstanding that the company had been dissolved. The Tribunal were prepared to infer, from such evidence as they had, that the liquidator had power to give such consent, but were prepared to hear evidence directly on the point if necessary. Assuming that formality of the surrender was met, then at that time self-evidently there was no possibility that the losses of MSB could be utilised, so M&S could claim them by way of group relief.

175. For MSG the latest point at which a group relief claim was made in relation to losses arising in the self-assessment years was on 12 December 2007 (also the date of the third group relief claim in respect of MSB). This was after the liquidator of MSG had settled all third party liabilities of MSG and had made the final distribution of the company's assets to shareholders, and two days before it was dissolved and removed from the commercial registry. In those circumstances it seems to us that at that time, and on any common sense basis, the possibility that the losses could be utilised in the future falls definitely on the "fanciful" side of the line.

176. On the basis of our decision as to the validity of the group relief claims we are not required to consider whether the no possibilities test was satisfied as at the date of the second group relief claims in relation to losses of MSG and MSB arising in the self-assessment years (that is, as at 20 March 2007). If it were a matter which required our decision, we would agree with the findings of the Tribunal. MSG had ceased to trade in August 2001, and had been in liquidation since October 2006. Under German law a minimum period of one year must pass following public notice of the liquidation before a company can be dissolved, so that there was then at least a seven month period before the company could be dissolved. The liquidator's obligations are to proceed with the settlement of liabilities and distribution of surplus assets so as to enable the company to be dissolved. The shareholders can terminate that process. In this instance the shareholder of MSG was M&S itself which was claiming the losses by way of group relief pursuant to a consistent course of action which began in 2000. In these circumstances there was no real possibility that the losses would be utilised in the future – such possibility as did exist is fairly described as fanciful.

The quantum of losses for which relief should be given

177. The final issue we have to deal with concerns the method to be used to calculate the amount of losses for each year which can be claimed by M&S by way of group relief. This is an issue, of course, only if, as the Tribunal found, and as we in turn find, in principle M&S has made valid group relief claims for losses which are eligible for relief in accordance with the ECJ Judgment.

178. The parties agreed the underlying figures for the losses which satisfied the no possibilities test, but they could not agree the amounts which were eligible each year for group relief, principally, as will appear, because of the effect in the different tax systems of timing differences in the taxation of certain receipts or deductions: that effect shifted the amounts of losses between different years. The parties returned to the Tribunal, which gave its decision on the matter in the Quantification Decision, and HMRC have appealed against that decision.

179. Little guidance is given on this aspect of the case by the ECJ Judgment. We remind ourselves of the relevant passages:

(1) As we have noted in paragraph 26 above, the ECJ was proceeding on the basis that the losses must be computed on a UK tax basis, which was the agreed basis on which the parties had brought the proceedings. However, that observation related to the losses referred to earlier in paragraph 22 of the Judgment – namely the claim for group relief under Schedule 17A "in respect of losses incurred" in the foreign subsidiaries. The fact that the claim was for losses as so calculated does not mean that the relief to which M&S would eventually be found to be entitled was to be by reference exclusively to the amount of the losses as so calculated.

(2) Paragraph 32 of the ECJ Judgment identifies the cash advantage to the group of the set-off of losses pursuant to group relief. And paragraph 33 identifies the exclusion from such relief of losses of a foreign subsidiary as being such 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 is unclear in this

passage whether the ECJ is referring to losses as calculated for tax purposes in accordance with the law of the residence of the other group company (M&S in the present case) or as calculated for tax purposes in accordance with the law of the residence of the loss-making subsidiary or on some other basis (for instance in accordance with the statutory accounting basis ascertained by the application of international accounting standards).

(3) Paragraph 34 concludes that the refusal of group relief constituted a restriction on the freedom of establishment in that it applies a different treatment for tax purposes to losses incurred by resident and non-resident subsidiaries. Read literally, this might suggest that a restriction on the freedom of establishment is always to be found unless the tax treatment is identical, so far as concerns group relief, for resident and non-resident subsidiaries with the result that precisely the same reliefs ought to be given as if the non-resident subsidiary had in fact been resident, with calculations being effected accordingly.

(4) However, such a restriction is permissible if it pursues a legitimate objective and is appropriate to attaining that objective and does not go beyond what is necessary. The ECJ held that the exclusion of group relief for the losses of a foreign subsidiary did pursue a legitimate objective but that the blanket exclusion of such losses went too far.

(5) The UK government and others put forward three justifications for the exclusion of foreign losses from group relief (see paragraph 43 of the ECJ Judgment):

a. The need to protect a balanced allocation of powers to impose taxes between Member States. To give companies the option to have their losses taken into account in one or other Member State might make it necessary to apply to the economic activities of companies established in one State only the tax rules of that State both in relation to profits and losses.

b. The risk of losses being taken into account twice.

c. If losses were not taken into account in the Member State of the subsidiary's residence there would be risk of tax avoidance.

(6) In the light of those three factors, it was held that the exclusion of non-resident subsidiaries from the group relief provisions did pursue legitimate objectives. The question therefore was whether the total exclusion of relief was a proportionate response.

(7) In paragraph 55, the ECJ set out the extent to which the group relief provisions went beyond that which was necessary to attain the legitimate objective. Those provisions went too far where

a. The non-resident subsidiary has exhausted the possibilities available in its home state of "having the losses taken into account" for the accounting period to which the relief relates and earlier periods; and

b. There is no possibility for those losses to be taken into account in the home state for future periods.

(8) In other words, the "losses" should attract group relief where they are unrelieved and incapable of relief in the home state of the subsidiary.

(9) Finally, in paragraph 56 the ECJ said this:

> "56 Where, in one Member State, the resident parent company demonstrates to the tax authorities that those conditions [the no-possibilities test] are fulfilled, it is contrary to Articles 43 EC and 48 EC to preclude the possibility for the parent company to deduct from its taxable profits in that Member State the losses incurred by its non-resident subsidiary."

(10) That is reflected in the *dispositif* in paragraph 59.

180. It is worth observing at this stage that the ECJ did not focus on the sort of problem which we are addressing about the correct methodology for ascertaining the quantum of the group relief claim. It seems to us that the ECJ did not have in mind that the different tax systems would throw up markedly different results (on a year by year basis) particularly in relation to the timing of when particular items of expenditure or receipt fall to be taken into account for tax purposes. It was using the concept of "loss" at a higher, or more abstract, level without drawing a distinction between the different systems. The way the ECJ dealt with three factors prayed in aid by the UK government illustrate this. Thus in each case, reference is made to losses – transferring losses or using losses twice, in a way which suggests that there is something described as a "loss" which can be objectively ascertained and used (without adjustment or recalculation) in one Member State or the other.

181. In the light of that approach by the ECJ, its resolution of the questions before it makes perfectly good and simple sense. The losses can be viewed as losses in the home State and the question can be asked whether they have been or might possibly be relieved. If so, they cannot attract group relief. Conversely, if they have not been and cannot possibly be relieved, they can be viewed as losses incurred by a UK resident group company and therefore may attract group relief.

182. It is apparent that the whole thrust of the ECJ Judgment is to ensure that losses which arise in the home State and which are not capable of being relieved in the home State should be available for transfer, by way of group relief, to the State of residence of another group company. Quite clearly, the home State can only ever relieve losses which arise under its own tax code. In addressing the losses which have not been relieved or in relation to which there is no possibility of relief, it can be argued that the ECJ must have had in mind only amounts calculated as losses in any relevant period according to that code. On this argument, it cannot have had in mind the possibility of there being some other sort of "losses" (e.g. a larger loss as calculated for the purposes of the UK tax regime) which were not losses under that code and thus not relievable in the home State on any footing.

183. The difficulty for us arises because the ECJ did not address the different amounts of loss – in the sense of loss for tax purposes – which exist in any relevant period depending on which tax regime is applied. There is no point in attempting to apply a literal reading of the ECJ Judgment because we know that the ECJ did not address the question. Rather, we have to address the question as one of principle taking account of the decisions by the ECJ (i) that the group relief provisions pursue legitimate objectives and (ii) that it is excessive to deny relief where the losses are not and cannot be utilised in the home State.

184. At paragraph 51 of the Substantive Decision the Tribunal outlined the approach which it considered should be taken: the no possibilities test must be applied to losses computed according to the local tax law of the foreign surrendering group company; it is a question of local law whether such losses so computed can be utilised. Then they said this:

> "We agree with Mr Ewart that these should then be converted into sterling and recomputed in accordance with UK tax principles. If this were not done a non-resident subsidiary could obtain a greater amount of relief for losses than a UK subsidiary in the same circumstances, which goes further than necessary to give effect to the no-possibilities test."

185. The Tribunal considered several methodologies (Methods A to F). Methods A to C were raised at the original hearing. In the light of the passage just quoted from the Substantive Decision, Methods D to F were formulated as attempts to apply to the computation of losses, and were considered in the Quantification Decision. We need to say a little about each of those Methods.

186. Method A: losses are calculated according to the foreign tax rules: they are utilised in accordance with local law. The unutilised losses (as so calculated) are subject to a group relief claim.

187. Method B: is not advocated by any party. It sought to convert local losses into a schedular approach consistent with the UK system but proved overly cumbersome and complicated.

188. Method C: losses are calculated according the UK tax rules; they are utilised in accordance with UK rules as if the foreign companies were subject to UK tax.

189. Method D is far more sophisticated: losses are calculated according to the foreign tax rules to determine the extent to which they satisfy the no possibilities test; the losses which satisfy that test (and which are therefore eligible for group relief) are recalculated on a UK tax basis, and relief given to the extent that they equal or are less than the amount of losses for the year as calculated locally, and if in a year the losses calculated on a UK tax basis exceed the losses as calculated locally, the excess is carried forward or back to those years where the locally calculated losses exceeded the UK calculated losses. It has always been the position of M&S that it would be content with any of Methods A to E inclusive. It is very content with the method selected by the Tribunal, Method E, which Miss Shaw submits is the right answer. However, she submits that Method D also achieves a fair result. M&S therefore reserve the right to argue the point if the matter goes further. However, it is content with Method E and accepts that it is consistent with the Tribunal's approach. Mr Ewart does not support Method D. We do not, therefore, consider it further.

190. Method E: this was the method which found favour with the Tribunal. Under this method, losses for each year are calculated as follows (using MSG as an illustration):

(1) Losses and profits were stated for each year as the tax losses or profits computed for German tax purposes;

(2) Those German tax losses which were utilised in accordance with German tax law against profits in later years were treated as utilised on a “first in, first out” basis, so that losses in the first year were treated as utilised first, then losses in the second year and so on in sequence. In the result, for MSG this meant that there were no losses for German tax purposes for years 1996 and 1997, and there was some reduction in the losses in 1998;

(3) The losses and profits were then re-stated for each year on a statutory accounting basis (that is, reversing the process by which the statutory accounts prepared in accordance with relevant accounting standards would have been adjusted to give the losses and profits as they were required to be computed for German tax purposes);

(4) The resulting statutory losses and profits were then adjusted so as to compute them for UK tax purposes;

(5) Those losses (i.e. the amount of the foreign tax losses) which had been utilised against profits in later years were then deducted from losses in the earlier years (on the same “first in, first out” basis);

It should be noted that this Method does not allow a claim for group relief to be made unless there is, at some stage, a local loss of equivalent or greater amount which has not been relieved. The Method is designed to throw the local loss in any given accounting period into the years where the corresponding UK loss is recognised, although as we shall see, matters are not quite that straightforward.

191. The outcome of applying Method E was that MSG had a small amount of losses (as computed for UK tax purposes) in 1997, and in each of the subsequent years the amount of “UK” losses differed from the amount of the “German” losses for the corresponding year, sometimes exceeding and sometimes falling short of the amount of the “German” losses. In some years the difference was marked: in 2000 the “German” losses exceeded £30m whilst the “UK” losses were less than £16m; in 2002 there were no “German” losses (rather, a profit of £2.5m) whilst the corresponding calculation gives a “UK” loss of £15.8m. In aggregate the amount of the “German” losses was £81,458,696 and the amount of the “UK” losses shown as available for group relief was £74,422,323.

192. Method F: this was proposed before the Tribunal by HMRC. Under this method, one proceeds as follows:

a. Take the foreign losses to identify the quantum and years in which the losses arise after utilisation on the basis of local law (these are the losses identified under Method A).

b. For each year reverse the local tax adjustments and apply UK tax adjustments to calculate UK equivalent losses.

c. For each year take the lower of the Method A loss and the UK equivalent loss as the amount available for group relief.

193. In paragraph 6 of the Quantification Decision, the Tribunal noted Mr Ewart's arguments to the effect that there can be no restriction in denying group relief where the subsidiary did not incur any loss in its home state in a particular period and that it is not contrary to Article 43 to preclude the parent company from deducting more than the foreign loss. They then expressed, in paragraphs 7 and 8, their clear view about the correct principles to apply:

> "7. We consider that the principle by which the full relief should be given is clear. The difference in the amount and timing of the losses between local tax law (Method A) and UK tax law (Method C) is a necessary consequence of the ECJ's decision. The no-possibilities test has to be applied to the local law losses, and the conversion of the losses to which the no-possibilities test applies is necessary to ensure that greater losses are not available than would be the case if the losses were incurred by a UK resident subsidiary. If the subsidiary had been in identical circumstances but had been UK resident the losses would fall in the periods shown by Method C. Once you move from identifying the local losses (computed under local rules) to identifying their equivalent under UK rules, you also have to move from local timing of recognition to UK timing of recognition. The difference in the total losses for all relevant years is a difference caused by differences in computation that has to be accepted. The timing difference that Mr Ewart contends denies group relief is not an ordinary timing difference that might result in denial of group relief in a wholly domestic situation, for example because there are no profits in the parent company against which the subsidiary's loss can be relieved; it arises because the company has chosen to establish a foreign subsidiary rather than a UK subsidiary. If losses are not allowed in these circumstances there is a difference in treatment of the two situations according to whether you establish a UK or a German subsidiary. That is precisely the restriction that the ECJ said was a breach of Article 43. If the losses have been identified as no-possibilities losses, it must be an unjustified restriction to prevent their relief because of different German and UK recognition rules.
>
> 8. Accordingly we do not agree with Mr Ewart's contentions that only the lower of the local and UK amount of losses for each year is allowable, which we consider is too literal a reading of what the ECJ decided. For example, it results in no group relief for DSG for the period ended 31 March 2002 when the UK equivalent amount of losses is over £15m. The simplest way of removing the restriction is to apply Miss Shaw's Method E which is closely based on our previous decision, and which we consider is the right approach. We attach a spreadsheet setting out the figures resulting from the application of this Method."

194. We turn now to the arguments before us and the criticism of the Tribunal.

195. Mr Ewart points out that the consequence of the Tribunal's reasoning is that group relief calculated according to UK tax loss recognition rules is available for accounting periods in which the non-resident subsidiary has either no losses which satisfy the no possibilities test or a lesser amount of losses. This he submits goes further than required by the ECJ Judgment. He refers to paragraph 33, identifying the loss there referred to with the loss as calculated in accordance with local law.

196. Applying Mr Ewart's approach to the circumstances of MSG it is the case, by way of illustration, that in the year 2002 nothing would be allowed by way of group relief in relation to MSG, since there were no "German" losses in that year; in the converse case (as in the year 2000) relief would be limited to the amount of the "UK" losses (£16m approx.) rather than the amount of the "German" losses for that year (£30m approx.).

197. Mr Ewart argued that the differences between the numbers arises because of the different loss regimes which themselves are a consequence of the feature that there is no harmonisation of corporation tax within the European Union, each Member State having sovereignty to set its own tax rules in this respect, and that disadvantages that result from the operation or conjunction of different national tax systems do not contravene Community law, as established by Case C-194/06 *Orange European Smallcap Fund* [2008] ECR I-03747. The Tribunal had been in error in trying to ameliorate such differences, and in doing so were going far beyond the scope of the relief envisaged by the terms of the ECJ Judgment: the essence of the ECJ Judgment is to allow relief for foreign losses where otherwise there would be a breach of Articles 43 and 48, but there is no such breach if relief is denied for amounts exceeding the foreign losses.

198. He also relies on what was said by Advocate General Geelhoed in Case C-374/04 *Test Claimants in Class IV of the ACT Group Litigation v HMRC* at paragraphs 35 to 40. What the AG was saying in summary was that there are two types of restriction that you can identify: one that is caused solely by, let us say, the UK tax system, and that is a restriction that can be contrary to Article 43, but there are also restrictions, quasi restrictions, that are caused because there are different legal systems in different Member States. That, the AG says, is not something that is contrary to Article 43.

199. It is necessary, therefore, for us to say something about the way in which differences in the computations of UK losses and, say, German, losses will occur (speaking of losses as they are computed for an accounting period for respective tax purposes). There are some differences which occur because of differences in principle, so to speak, in the respective tax systems: a particular item of expenditure is tax deductible in one system and not in another, or, conversely, a particular item of receipt is taxable in one system and not in another (although these differences are not likely to be highly significant as between tax systems in sophisticated commercial countries). There are other differences which occur because of differences in timing – in principle each system allows a deduction for an item of expenditure or taxes an item of receipt, but it is spread over more than one accounting period. Most strikingly this difference in timing is seen in the treatment of the deduction for certain types of expenditure of a capital nature (and the treatment of the corresponding receipt on the disposal of the capital asset in question): in some tax systems such expenditure is deductible as and to the extent that it is depreciated for accounting purposes over the anticipated lifetime of the asset on which the expenditure has been incurred; in others (including the UK) it is deductible under a system of capital allowances, which may have the effect of accelerating the deduction as against the position where the deduction is allowed in accordance with accounting depreciation.

200. It should therefore not be a matter of surprise that, taking the losses of MSG over the whole of the relevant period, the aggregate amount of losses computed

for German tax purposes is within less than ten per cent of the aggregate amount of losses as they are computed for UK tax purposes. Taking year by year, however, the differences are, on occasion, very significant, reflecting, so it would seem, the marked effect of timing differences. In the case of MSB there is a greater disparity in the aggregate amount of losses as computed under each system but less disparity on a year by year basis.

201. Mr Ewart describes the differences between the UK loss relief regime and the German and Belgian loss relief regimes as classic examples of the disadvantages which arise purely as a consequence of the parallel exercise of fiscal sovereignty by Member States. He says that such disadvantages do not contravene Community law and the Tribunal was in error in seeking to ameliorate them. As we understand this argument, it is permissible (and this is clearly correct) for the UK and Germany or Belgium to have different regimes for loss relief; and whilst it is not permissible for the UK to refuse group relief in relation to foreign losses calculated in accordance with the foreign loss regime (to the extent that they are unutilised and unutilisable locally), Community law does not require one to go further; otherwise the group would obtain excessive relief and thus override the principle of fiscal sovereignty.

202. We are not entirely clear whether Miss Shaw has altogether abandoned Methods A and C. We do not think that either of them can be the correct approach. Method A is open to the objection that where the underlying issue is the freedom of establishment, it does not give the result that would ensue were the foreign group company in fact a UK resident group company carrying on the same activity. To give that result it is necessary to re-state the losses of the foreign group company as they would be computed were it instead such a UK resident group company. This was common ground between the parties and was the basis of the reference made to the ECJ and in turn was accepted by the Tribunal. Method C meets this objection, but does so at the cost of ignoring the losses as they are calculated for local tax purposes, which then presents difficulties in determining whether (and if so, the extent to which) they are utilised or capable of being utilised locally. In short, both Methods A and C disregard what is the nub of the difficulty of this question, namely taking account of, or reconciling, losses which are computed differently under different tax regimes, and doing so for the different purposes of ascertaining whether for any year losses have been or can be utilised and then giving group relief to the extent that that is not the case.

203. Miss Shaw describes the Tribunal’s approach as one which was to move losses incurred in one period locally to a different (earlier or later) period under UK rules. In other words, switching between UK and local rules produced timing differences as to the year in which losses were recognised. This would not occur if the rules of a single State were applied. She gives examples of these timing differences which will be familiar, for instance the different treatment of capital expenditure already identified, or the provision for future rent (where in the UK such a provision is deductible when it is charged in the accounts whereas in Germany and Belgium the deduction is given when the rent is actually paid).

204. The timing differences can give rise to extreme results. Miss Shaw provides these examples:

(1) In Year 1 a foreign company has an accounting loss of £100 due to a £100 provision for future rent on an empty property. The local tax loss is £0 as

the provision is only allowable when the rent is paid in cash in the following year. For UK tax purposes the provision would be allowable in Year 1 and therefore a UK basis tax loss of £100 will arise in Year 1;

(2) Assume in Year 2 there is – disregarding the rent – a nil accounting profit and the company is liquidated by the end of the year. As the rent will have been paid in Year 2 the foreign tax loss will be £100. However, on a UK tax basis there is no loss in Year 2 as the deduction for rent will have been taken in Year 1;

(3) Thus the tax loss in both jurisdictions is £100 but is taken in Year 1 in the UK and Year 2 in the foreign jurisdiction

205. As we understand Mr Ewart's position, group relief could not be obtained for Year 1 because there is no foreign loss; and relief could not be claimed for Year 2 because there is no loss computed in accordance with UK rules and therefore nothing for the group relief claim to bite on. That might be thought to be a surprising result and to indicate that timing differences have to be reflected in the way that group relief has to operate in the context of foreign losses. This, we think, is the point which the Tribunal made when it said that once you move from identifying the local losses (computed under local rules) to identifying their equivalent under UK rules, you also have to move from local timing of recognition to UK timing of recognition.

206. Miss Shaw points out (as the Tribunal noted) that if M&S were denied the benefit of the timing differences, there would be a difference in treatment according to whether M&S chose to establish a UK subsidiary or a foreign subsidiary. She submits that the Tribunal's decision that the losses available for surrender should not be reduced by timing differences is correct. HMRC's approach of taking the lower of the losses computed on a local or UK basis year by year is wrong because it would allow the discriminatory restriction to persist, and as we have indicated by reference to MSG for the years 2000 and 2002 the effect can be very marked. As the Tribunal states, the effect of such an approach is to place M&S in a worse situation than if it had established the Belgian and German subsidiaries in the UK.

207. Miss Shaw then says that the purpose of restating the local losses in accordance with UK principles is to put M&S in the same situation as if it had established a UK subsidiary. The period in which the losses are taken is an integral and necessary part of that conversion.

208. To describe in these terms the purpose of restating the losses as UK losses is, however, to overstate the position and in a real sense to beg the question at issue. The restatement by itself has no free-standing purpose: it is required only if and to the extent that it plays a part in eliminating an inadmissible infringement of Article 43. And it is against that factor, the need to ensure that there is no infringement of Article 43, that the correctness or otherwise of any given proposed methodology must be judged.

209. Miss Shaw's example is, of course, supportive of her position. However, if we modify the example and assume that in Year 2 there is an accounting profit of £100 before taking account of the rental deduction, there is no tax loss in the foreign jurisdiction and a profit of £100 in the UK. It is true that a deduction will be taken in the foreign jurisdiction in Year 2 for the rent, but it does not result in a

loss. Accordingly, the overall position in the UK is that there is a tax loss in Year 1 with a corresponding profit (or on different figures, a knock-on effect for the profit and loss account) in Year 2, whereas in the foreign jurisdiction there is no loss at all in either Year 1 or Year 2.

210. How does group relief work in this modified example? Mr Ewart's approach would, we imagine, not allow group relief. In Year 1, as before, there is no foreign loss. In Year 2, the position is *a fortiori* the original example because there is no loss calculated in accordance with either set of computational rules. In this situation Mr Ewart's approach gives a reasonable result.

211. The result must surely be that there is no group relief allowable under Method E either. It cannot, we think, be said that group relief should be allowed as if the foreign subsidiary were in fact a UK subsidiary. That would be to allow a group relief claim in Year 1 of £100 without that relief being reflected in Year 2 – in Year 2 the subsidiary, if it were a UK subsidiary, would have a tax profit of £100 but the foreign subsidiary would not show a tax profit at all. Consideration of these two examples demonstrates, in our view, that a group relief claim can only reflect an actual loss in the foreign subsidiary, but that that loss does not have to occur locally in the same year as the relevant group relief claim.

212. Thus, in the modified example, there is no local loss at all which falls to be relieved locally or which can form the subject matter of a group relief claim. The timing differences in the recognition of the deduction (in the examples, deduction of the rent) have not resulted in a loss which is recognised locally and there is therefore nothing to be recognised at all, let alone in a different period, for UK tax purposes.

213. In the light of all of these considerations our conclusions are as follows.

214. First, in relation to differences in the calculation of losses and profits in the different jurisdictions which are nothing to do with timing differences, we accept Mr Ewart's submission that any disadvantages that result from the operation or conjunction of different national tax systems do not contravene Community law. In other words, it is correct to cap the amount of group relief available by the amount of any local loss to the extent that the differential in the amount of losses (UK and local) results from differences in principle between tax regimes, rather than from timing differences (a further limit being the amount of the relief available on that basis which has not been utilised locally and in respect of which there is no possibility that it will be utilised locally).

215. Although this aspect of quantum was not expressly addressed by the Tribunal, it is already taken account of in Method E, at least as we understand the methodology. As we have already said, it is inherent in Method E that group relief can only be claimed for the amount of the local losses; the Method is concerned with re-allocating losses (as an integral part of re-stating them for UK tax purposes) to periods where they arise for UK tax (and therefore UK group relief) purposes and does not result, overall, in a group relief claim being available for an amount in excess of the losses it is sought to re-allocate.

216. Where the losses calculated on a UK basis are greater than those calculated on the local basis (over whatever period of time you like to take), the group relief claims in aggregate cannot exceed the total losses calculated on the local basis (as the calculations for both MSG and MSB illustrate). It follows that Method E

already takes account of the possible differences in tax calculation which are not simply timing differences. If the local calculation gives a greater loss, the group relief claim is restricted to the amount of the loss calculated on the UK basis; and if the local calculation gives a smaller loss, the group relief claim is restricted to the actual loss of the foreign subsidiary,

217. In conclusion, our view is that the approach of the Tribunal is correct and that Method E provides the methodology which is most in tune with the ECJ Judgment and the principles which underlie it. The complexity of the solution is, it seems to us, a consequence of the complexity of trying to reconcile the necessary starting point (locally-computed losses) with the necessary finishing point (surrendering losses which are UK-computed) in a way which accords with the issue at the heart of the ECJ Judgment, namely eliminating any infringement of Article 43, and without the capricious results which ensue if timing differences are not taken into account

218. There is one final issue with which we must deal in relation to quantification and its consequences. Method E not only tells us what amounts may potentially be subject to a valid group relief claim but also tells us what year of account any re-allocation is to relate to. The spreadsheet for Method E shows an amount for each of the years 1997 to 2002 (for MSG) and for the year 2001 (for MSB) which is available for group relief. It is important to note that the claim for group relief relates to the year in respect of which there is an amount available for relief. The fact that the local loss arises in a later year does not alter that position. Thus, there is a claim for group relief in respect of MSG for 1997 even though there was no local loss in that year. A claim for that period had to be made, in accordance with our decision on the substantive issues, within the time limit applicable under UK law for the making of group relief claims. Accordingly, where a claim is out of time, it cannot be made even if the local loss was suffered in a year of account which falls within the time limit for making a claim. For example, the claims for 1997 (being a pay and file year) were out of time, and since M&S should not, in our judgment, specially be allowed to make a late claim, no relief is available for such losses.

Result

219. Our conclusions in summary are as follows:

(1) In relation to the self-assessment years (years to 31 March 2000, 2001 and 2002) for losses of both MSG and MSB, M&S is entitled to claim group relief: valid group relief claims were made, on the basis that sequential claims are effective, claims were made within time limits, and the latest claims were made after the no possibilities test had become satisfied. The quantum of the claim is to be ascertained under Method E. HMRC's appeal on this issue is dismissed.

(2) In relation to the pay and file years, for losses of MSG for years to 31 March 1998 and 1999, M&S is not entitled to claim group relief. This is on basis that, in relation to the claims which were made in time, the no possibilities test was not satisfied at the date of the claims; later claims made were outside the relevant time limits, and M&S should not be allowed specially to make a claim outside those time limits. We differ from the Tribunal on this point. HMRC's appeal on this issue is allowed.

(3) In relation to the pay and file year to 31 March 1997, for losses of MSG, and for years to 31 March 1998 and 1999, for losses of MSB, M&S is not entitled to claim group relief. This is on basis that the claims were made outside the relevant time limits, and M&S should not be allowed specially to make a claim outside those time limits. We differ from the Tribunal on this point. HMRC's appeal on this issue is allowed.

(4) If we are wrong on our general point ((1) above) as to M&S's right to make sequential group relief claims, so that it is necessary to look at the separate group relief claims, then the no possibilities test was not satisfied at the time of first group relief claims in respect of years 2000 and 2001 for both MSG and MSB (claims made 24 September 2001) or year 2002 for both MSG and MSB (claims made 26 March 2004), but was satisfied at the time of the second and subsequent group relief claims in respect of those years for both MSG and MSB. We agree with the Tribunal on this point, and HMRC's appeal on this issue is dismissed.

Mr Justice Warren

The President

Edward Sadler

Upper Tribunal Judge

Release Date: 21 June 2010

ANNEX

Extracts from Schedule 18, Finance Act 1998

Claim to be included in company tax return

67 (1) A claim for group relief must be made by being included in the claimant company's company tax return for the accounting period for which the claim is made.

(2) It may be included in the return originally made or by amendment.

Content of claims

68 (1) A claim for group relief must specify—

(a) the amount of relief claimed, and

(b) the name of the surrendering company.

(2) The amount specified must be an amount which is quantified at the time the claim is made.

Claims for more or less than the amount available for surrender

69 (1) A claim for group relief may be made for less than the amount available for surrender at the time the claim is made.

(2) A claim is ineffective if the amount claimed exceeds the amount available for surrender at the time the claim is made.

(3) For these purposes the amount available for surrender at any time is calculated as follows.

First step

> Determine the total amount available for surrender under section 403 of the Taxes Act 1988—
>
> > (a) on the basis of the information in the company's company tax return, and
> >
> > (b) disregarding any amendments whose effect is deferred under paragraph 31(3).

Second step

> Then deduct the total of all amounts for which notices of consent have been given by the company and not withdrawn.

(4) Where one or more claims are withdrawn on the same day as one or more claims are made, the withdrawals are given effect first.

(5) Where more than one claim is made on the same day, and the claims together take the amount claimed over the limit of what is available for surrender, [an officer of Revenue and Customs] may determine which of the claims is to be ineffective.

(6) The power under sub-paragraph (5) shall not be exercised to any greater extent than is necessary to bring the total amount claimed within the amount available for surrender.

Consent to surrender

70 (1) A claim for group relief requires the consent of the surrendering company.

…………

(3) The necessary consent or consents must be given—

> (a) by notice in writing,
>
> (b) to the officer of the Board to whom the surrendering company makes its company tax returns,
>
> (c) at or before the time the claim is made.

Otherwise the claim is ineffective.

(4) A claim for group relief is ineffective unless it is accompanied by a copy of the notice of consent to surrender given by the surrendering company.

……..

Notice of consent

71 (1) Notice of consent by the surrendering company must contain all the following details—

> (a) the name of the surrendering company;
>
> (b) the name of the company to which relief is being surrendered;
>
> (c) the amount of relief being surrendered;
>
> (d) the accounting period of the surrendering company to which the surrender relates;
>
> (e) the tax district references of the surrendering company and the company to which relief is being surrendered.

Otherwise the notice is ineffective.

(2) Notice of consent may not be amended, but it may be withdrawn and replaced by another notice of consent.

(3) Notice of consent may be withdrawn by notice to the officer of the Board to whom the notice of consent was given.

(4) Except where the consent is withdrawn under paragraph 75 (withdrawal in consequence of reduction of amount available for surrender), the notice of withdrawal must be accompanied by a notice signifying the consent of the claimant company to the withdrawal.

Otherwise the notice is ineffective.

(5) The claimant company must, so far as it may do so, amend its company tax return for the accounting period for which the claim was made so as to reflect the withdrawal of consent.

Notice of consent requiring amendment of return

72 (1) Where notice of consent by the surrendering company is given after the company has made a company tax return for the period to which the surrender relates, the surrendering company must at the same time amend its return so as to reflect the notice of consent.

(2) Where notice of consent by the surrendering company relates to a loss in respect of which relief has been given under section 393(1) of the Taxes Act 1988 (carry forward of trading losses), the surrendering company must at the same time amend its company tax return for the period or, if more than one, each of the periods in which relief for that loss has been given under section 393(1) so as to reflect the new notice of consent.

For this purpose relief under section 393(1) is treated as given for losses incurred in earlier accounting periods before losses incurred in later accounting periods.

(3) The time limits otherwise applicable to amendment of a company tax return do not prevent an amendment being made under sub-paragraph (1) or (2).

(4) If the surrendering company fails to comply with sub-paragraph (1) or (2), the notice of consent is ineffective.

Withdrawal or amendment of claim

73 (1) A claim for group relief may be withdrawn by the claimant company only by amending its company tax return.

(2) A claim for group relief may not be amended, but must be withdrawn and replaced by another claim.

Time limit for claims

74 (1) A claim for group relief may be made or withdrawn at any time up to whichever is the last of the following dates—

> (a) the first anniversary of the filing date for the company tax return of the claimant company for the accounting period for which the claim is made;

(b) if notice of enquiry is given into that return, 30 days after the enquiry is completed;

(c) if after such an enquiry the Inland Revenue amend the return under paragraph 34(2), 30 days after notice of the amendment is issued;

(d) if an appeal is brought against such an amendment, 30 days after the date on which the appeal is finally determined.

(2) A claim for group relief may be made or withdrawn at a later time if the Inland Revenue allow it.

(3) The time limits otherwise applicable to amendment of a company tax return do not apply to an amendment to the extent that it makes or withdraws a claim for group relief within the time allowed by or under this paragraph.

(4) The references in sub-paragraph (1) to an enquiry into a company tax return do not include an enquiry restricted to a previous amendment making or withdrawing a claim for group relief.

An enquiry is so restricted if—

(a) the scope of the enquiry is limited as mentioned in paragraph 25(2), and

(b) the amendment giving rise to the enquiry consisted of the making or withdrawing of a claim for group relief.

Reduction in amount available for surrender

75 (1) This paragraph applies if, after the surrendering company has given one or more notices of consent to surrender, the amount available for relief is reduced to less than the amount stated in the notice, or the total of the amounts stated in the notices, as being surrendered.

(2) The company must within 30 days withdraw the notice of consent, or as many of the notices as is necessary to bring the total amount surrendered within the new amount available for surrender, and may give one or more new notices of consent.

(3) The company must give notice in writing of the withdrawal of consent, and send a copy of any new notice of consent—

(a) to each of the companies affected, and

(b) to the Inland Revenue.

(4) If the surrendering company fails to act in accordance with sub-paragraph (2), the Inland Revenue may by notice to the surrendering company give such directions as they think fit as to which notice or notices are to be ineffective or are to have effect in a lesser amount.

This power shall not be exercised to any greater extent than is necessary to secure that the total amount stated in the notice or notices is consistent with the amount available for surrender.

(5) The Inland Revenue must at the same time send a copy of the notice to the claimant company, or each claimant company, affected by their action.

(6) A claimant company which receives—

> (a) notice of the withdrawal of consent, or a copy of a new notice of consent, under sub-paragraph (3), or
>
> (b) a copy of a notice containing directions by the Inland Revenue under sub-paragraph (4),

must, so far as it may do so, amend its company tax return for the accounting period for which the claim is made so that it is consistent with the new position with regard to consent to surrender.

(7) An appeal may be brought by the surrendering company against any directions given by the Inland Revenue under sub-paragraph (4).

(8) Notice of appeal must be given—

> (a) in writing,
>
> (b) within 30 days after the notice containing the directions was issued,
>
> (c) to the officer of the Board by whom the notice was given."