



Brussels, 18.5.2021
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COMMISSION RECOMMENDATION

of 18.5.2021

on the tax treatment of losses during the COVID-19 crisis

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THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 292 thereof,

Whereas:

- (1) The COVID-19 outbreak has prompted unprecedented action at national and Union level to support the EU economy and facilitate its recovery. The majority of short-term crisis response measures seek to ensure that businesses have sufficient cash flow.
- (2) Small and Medium sized Enterprises (SMEs)¹ in particular have been badly hit by the public health measures as they are often less able to absorb or finance losses than larger companies. SMEs are also more likely to be operating in business sectors that have had to close due to public health measures such as hotels, restaurants, cafés and bars.
- (3) Many jurisdictions have acted quickly to relieve the immediate tax burden on businesses with appropriate support measures, a considerable part of which has been subject to Union State aid rules, in particular the new State Aid Temporary Framework². While the most common type of tax measure to enhance business cash flow has been the deferral of tax payments, changes to loss-offset provisions have also been an important tax policy tool.
- (4) The Member States usually permit three main ways of treating losses for tax purposes. Losses can normally be (a) used in the current accounting period in which they arise so that no tax is due in that period. In addition, excess losses can either be: (b) carried forward and set against the next available future profits to reduce tax liability; or, in some Member States, (c) carried back and set against total profits in the preceding tax year or up to a number of preceding years to generate a refund of tax previously paid.
- (5) As a policy measure, loss carry forward is less useful to immediately help struggling businesses, because the taxpayer will only get the liquidity benefit when they are profitable again and liable to tax. Losses from previous years can be used in the current accounting period but this would not free up any liquidity unless a taxpayer is profit making. Loss carry back is much more valuable to businesses affected by the crisis because it results in a refund of taxes paid in previous tax years and provides additional liquidity to companies. It would, in particular, benefit SMEs.

¹ For a definition of an SME see Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises, OJ L 124, 20.5.2003, p. 36,

² Communication from the Commission - Temporary framework for State aid measures to support the economy in the current COVID-19 outbreak (OJ C 91, 20.3.2020, p. 1), as amended by Commission Communications C(2020) 2215 (OJ C 112, 4.4.2020, p. 1), C(2020) 3156 (OJ C 164, 13.5.2020, p. 3), C(2020) 4509 (OJ C 218, 2.7.2020, p. 3), C(2020) 7127 (OJ C 340, 13.10.2020, p. 1) and C(2021) 564 (OJ C 34, 1.2.2021, p. 6).

- (6) Loss carry back has the advantage of benefitting only the businesses that were profitable in the years before the pandemic, which means that it would support healthy businesses as a matter of principle. In practice, only businesses that were making a profit and paying taxes in the years prior to 2020 will be able to offset their 2020 and 2021 losses against those taxes. This ensures that the measure is targeted at businesses suffering as a direct result of the pandemic and public money is not spent trying to help private businesses that are failing for reasons unrelated to the crisis.
- (7) To ensure a targeted measure, the Member States that decide to allow carry back for more than one year, should restrict this to businesses that were not loss making in the previous years. Therefore, if a loss carry back is allowed for two or three years, this should be for businesses that were not loss making in 2019, 2018, or 2017.
- (8) The cost of such measures would mainly be a question of timing: the businesses get the money now when they most urgently need it, and they will not have to wait until they would be able to use their losses against future tax liability. The Member States will forgo tax revenue now, but they will receive tax revenue in the future from businesses that have remained afloat and will return to profitability. In addition, utilising loss carry backs will reduce existing loss carry forwards in future periods, which further mitigates the impact on tax revenues.
- (9) Some Member States have already introduced or announced measures allowing loss carry back for the 2020 tax year, which will allow taxpayers to carry back their 2020 tax losses against profits earned in previous fiscal years.
- (10) However, Member States usually operate divergent rules for the treatment of losses, which often creates an uneven playing field.
- (11) This recommendation to Member States on the domestic treatment of losses, drawing on best practice, could help level the playing field for companies across the Union.
- (12) This recommendation should apply for fiscal years 2020 and 2021, in order to help businesses during the COVID-19 crisis.
- (13) Member States should allow loss carry back for businesses to at least the previous fiscal year, i.e. until 2019. However, in order to enable taxpayers to utilise the full amount of their losses against taxes previously paid, the Member States may extend the carry back for up to the previous three years, i.e. until 2017. Smaller sized firms with lower profits can particularly benefit from this extended carry back period of up to three years.
- (14) The measure should be limited to prevent excessive impacts on national budgets. A limit of EUR 3 million per loss making fiscal year would provide valuable support for smaller companies in particular, while also ensuring that all taxpayers benefit to some extent.
- (15) The Commission recalls that where Member States introduce measures fulfilling the conditions to constitute State aid that is not exempt from the obligation of notification, they must notify such measures to the Commission in line with the procedures generally applicable to State aid,

HAS ADOPTED THIS RECOMMENDATION

1. SUBJECT MATTER AND SCOPE

With the aim to benefit businesses in the light of the economic situation caused by the COVID-19 pandemic, this Recommendation sets out a coordinated approach towards the treatment of losses for businesses incurred in fiscal years 2020 and 2021.

2. THE TAX TREATMENT OF LOSSES

Given the exceptional economic circumstances in the years 2020 and 2021, as a result of the COVID-19 pandemic, Member States should allow loss carry back for businesses to at least the previous fiscal year, i.e. at least 2019.

Member States may extend that period to allow loss carry back up to the previous three years, thus allowing companies to set off their losses referring to fiscal years 2020 and 2021 against already taxed profits in the fiscal years 2019, 2018, and 2017.

Member States should allow businesses to immediately claim the carry back of losses which they estimate to incur in fiscal year 2021, without the need for waiting until the end of the year.

3. LIMITATIONS

In order to limit the impact on national budgets, Member States should limit the amount of losses to be carried back. EUR 3 million per loss making fiscal year should be the maximum amount for the loss carry back.

If Member States allow the loss carry back up to 2017, eligible businesses should not have incurred losses in any of fiscal years 2019, 2018 and 2017.

4. FOLLOW-UP

Member States are requested to inform the Commission about the measures taken further to the present Recommendation, as well as on any changes made to such measures.

Member States are invited to discuss with the Commission their plans for providing loss carry back for businesses.

5. ADDRESSEES

This recommendation is addressed to the Member States.

Done at Brussels, 18.5.2021

For the Commission
Paolo GENTILONI
Member of the Commission

