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CJEU AG issues opinion on Dutch dividend withholding tax cases

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Advocate General (AG) Jääskinen of the Court of Justice of the European Union (CJEU) issued his opinion on 25 June 2015 in three joined cases involving the Dutch dividend withholding tax provisions. According to the AG, withholding tax imposed on a nonresident may not exceed the full individual income tax burden of a resident taxpayer. Where this is not achieved even after a tax credit has been granted by the residence state under the provisions of a tax treaty, it is then the responsibility of the source state to ensure that the impact of the withholding tax is "neutralized."

The compatibility with EU law of dividend withholding tax levied by one EU member state on shareholders resident in another EU member state has been an ongoing issue for several years; specifically, whether such taxes infringe the freedom of establishment and free movement of capital provisions in the Treaty on the Functioning of the European Union. The CJEU has ruled in previous cases that a foreign shareholder cannot be subject to a heavier tax burden than a similarly situated domestic shareholder. The three cases now before the CJEU should shed some light on the appropriate comparison to be made between cross-border and domestic situations.

Background and facts

When a Dutch resident company distributes dividends to its individual and corporate portfolio shareholders, Dutch dividend withholding tax is due at a rate of 15%. When dividends are paid to nonresident shareholders, the tax is considered a final levy, whereas when dividends are paid to Dutch resident shareholders, the 15% dividend withholding tax is neutralized because the shareholders can credit the tax against their individual or corporate income tax liability, as appropriate. This could lead to a more advantageous treatment of the dividend payment in domestic situations. The Dutch Supreme Court referred three cases to the CJEU in 2013 for a preliminary ruling on whether the Dutch tax treatment infringes EU law.

Two of the cases before the CJEU involve the Dutch dividend withholding tax levied on individual shareholders in Dutch companies, and the third involves the withholding tax levied on a French bank. The facts of the cases can be summarized as follows:

- *Miljoen* case: The taxpayer, a Dutch national who resided in Belgium, received dividends from Dutch companies and was subject to the 15% withholding tax. The taxpayer claimed a refund for the portion of the withholding tax that exceeded the income tax he would have paid had he been resident in the Netherlands.
- *X* case: In a similar case, a Dutch national resident in Belgium also was subject to a 25% Belgian income tax on the net dividends. The Dutch withholding tax was not included in the Belgian income tax base; Belgium refused to credit the Dutch withholding tax against the taxpayer's Belgian income tax liability, based on the provisions of the Netherlands-Belgium tax treaty.
- *Société Générale* case: A French bank received dividends from a Dutch company and was subject to Dutch withholding tax. Although the bank was able to credit the withholding tax against its French corporate income tax, it could not fully benefit from the tax credit because of losses incurred in France. Had the dividends been paid to a Dutch company, the 15% withholding tax still would have applied, but the Dutch recipient would have been able to deduct related expenses. The French bank, however, incurred both direct (e.g. interest on financing of the shares) and indirect (e.g. hedging) costs in relation to its investments, but these were not taken into account in the Netherlands, since the Dutch withholding tax is levied on a gross basis.

AG opinion

The main issue in the joined cases is how to make an appropriate comparison of the tax burden in cross-border and domestic situations. The three main possibilities are as follows:

1) Since dividend withholding tax is levied in both domestic and cross-border situations, there should be no difference in treatment;
2) The dividend withholding tax as a final levy in cross-border situations should be compared with the combined tax burden of dividend withholding tax and individual/corporate income tax in domestic situations; or
3) The dividend withholding tax as a final levy in cross-border situations should be compared with the effective dividend withholding tax burden in domestic situations.

AG Jääskinen discusses all three possibilities in his opinion. Since taxpayers in Dutch domestic situations always are entitled to some kind of relief for dividend withholding tax, the AG concluded that the tax burden on a dividend recipient in domestic situations at least should be included in the comparison. In principle, the AG suggests that the Dutch dividend withholding tax is incompatible with EU law because the tax always is fully neutralized when dividends are paid to resident taxpayers.

Ultimately, however, AG Jääskinen favored a comparison of the final 15% dividend withholding tax levied in a cross-border situation with the combined levy of dividend withholding tax and income tax in domestic situations. According to the AG, the comparison should be made on an annual basis, taking into account the dividends in the fiscal year in which they are distributed and all deductions and tax-free allowances that would be available to a domestic taxpayer. Under the approach, the full domestic tax treatment would be taken into account and Dutch law would be considered incompatible with EU law to the extent of any

difference between the tax burden that would arise in a domestic situation and the burden resulting from the imposition of the 15% flat rate dividend withholding tax.

Role of tax treaties

AG Jääskinen also addressed the role of tax treaties, indicating that the elimination of double taxation, as provided for in an applicable tax treaty, also needs to be taken into account. Arguments have been raised, on the one hand, that the mere fact that a treaty provides for the elimination of double taxation is sufficient to avoid discrimination and, on the other hand, that such elimination actually needs to be implemented. The AG suggested that, in itself, the possibility of applying a tax credit is insufficient and that the mechanism for granting the credit under the domestic law of the state of residence of the recipient is an important part of the analysis. The end result should be that the impact of the dividend withholding tax is fully eliminated. Most treaties, however, allow only an ordinary credit, i.e. the state of residence of the recipient is not required to grant a credit for more than the amount of the domestic tax on the income concerned. According to the AG, in principle, it is the source state's responsibility to ensure that full neutralization is achieved.

Comments

The CJEU now must issue its own ruling in the joined cases (the court is not obliged to follow AG Jääskinen's opinion), and the court's decision will be important, not only for the Netherlands, but for all EU member states. Reimbursement requests are pending before the tax authorities and courts of many member states—in the Netherlands alone, such requests total about EUR 8 billion.

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