New tax regulations impacting investment funds

Germany India Ireland Netherlands Switzerland

Germany

New tax regulations under AIFM-StAnpG—guidance from the German fiscal authorities

Eva Ernst
Senior Manager
Financial Services Tax
Deloitte

Till Westermeier
Manager
Financial Services Tax
Deloitte

At the second attempt, the AIFM Tax Adjustment Act (AIFM-StAnpG) came into force on 24 December 2013. The Federal Ministry of Finance (BMF) has issued a set of guidelines regarding, *inter alia*, the treatment of share classes, investment restrictions, allocation of expenses, distribution order, transitional arrangements and eligible assets.

Background—scope of application and changes

Modified scope of application

In general, the German Investment Tax Act (InvStG) is applicable for all UCITS and AIFs. Holding companies, institutions for occupational pension schemes, securitisation special purpose entities, venture capital companies and public sector capital investment companies are not subject to the InvStG.

> The taxation of mutual funds in its current form remains generally unchanged; however changes will be made in subareas

The taxation of mutual funds in its current form remains generally unchanged; however changes will be made in subareas. From a tax perspective, UCITS and AIFs only qualify as funds when the requirements of section 1, paragraph 1b of the InvStG are fulfilled. In other cases, funds are considered to be investment companies, for which the taxation for business partnerships or corporations applies, depending on the legal form of the entity concerned.

Changes

Domestic pension pooling/investment limited partnership

The open-ended investment limited partnership was introduced as a third form of an open-ended domestic investment fund. As an investment fund, it is exempt from trade tax and does not establish a domestic business premise for its investors.

The main objective of introducing an open-ended investment limited partnership was to create a transparent investment tool for DBA purposes that offers domestic pension scheme institutions the opportunity of a full or partial reduction or refund of foreign source taxes. German pension and retirement institutions should compare the advantages of this structure with schemes currently used.

Distributions

Distributions made after 23 August 2014 are to be primarily taken from earnings from the current and past fund financial years for tax reasons. A substance distribution, meaning repayment of capital, can only be made if all income and gains for the current year and prior years have already been distributed.

General transitional rules

The AIFM-StAnpG regulations are generally to be applied after 23 December 2013. The transition regulations state that investment funds which were launched before 24 December 2013 will be considered as investment funds until the end of the financial year that ends after 22 July 2016, as far as they continue to fulfil the previous requirements of an investment fund according to the old InvStG. The InvStG regulations in the version applicable on 21 July 2013 will continue to apply for the period from 22 July 2013 to 23 December 2013.

Cost allocation

Direct costs must be set off against the corresponding income if a direct economic link can be established. Subsequently the remaining expenses are considered to be 'general expenses' (*Allgemeinkosten*) and have to be deducted in three distinctive steps (Level 1 to 3), increasing the complexity factor.

- ***Level 1:*** 100% of the general expenses have to be allocated to their corresponding source of income based on the previous fiscal year, i.e. (1) DTT-sourced (tax-exempt real estate proceeds), (2) equity-sourced and (3) other assets
- ***Level 2:*** expenses have to be split within their 'category' between current income (e.g. rent, interest, dividends, manufactured dividends, gains/losses reclassified as DDI *"Finanzinnovationen"*) and realised gains/losses from disposal of investments (i.e. disposal of real estate after ten years, equity and other investments) on a pro rata basis
- ***Level 3:*** another allocation of general expenses to certain further sub-categories within their specific income category applies. The details are set out in BMF Circular dated 22 September 2014 and amended on 10 November 2014

Remaining expenses have to be deducted in three distinctive steps (Level 1 to 3), increasing the complexity factor

Share classes and income equalisation

The procedure for general expense allocation has to take into account income equalisation. Generally, the fiscal authority prefers a single expense allocation ratio for all share classes; newly issued share classes adopt the previous year's values of the existing entire sub-fund. Expense allocation ratios that differ at the share class level are only accepted by the fiscal authority if the difference is immaterial. So far, the only official statement is that a difference between classes deriving from currency hedging would be considered immaterial. As a simplification rule, the income equalisation values may be taken into account only for share classes for which the German tax reporting data is calculated and published according to section 5 of the InvStG (paragraph 1, sentence 1, points 1-3).

Start of calculation at fund launch

The launch of a new sub-fund also requires the determination of three types of assets—real estate, equity and other. Due to the lack of a prior year, the ratio of the average assets has to be based on the current fiscal year, as in previous legislation.
At Level 2, the costs are divided equally between current income and realised gains/losses from the disposal of investments.

Level 3 cannot be applied for newly launched funds. The fiscal authority would therefore accept any appropriate and coherent allocation criteria.

The fiscal authority prefers a single expense allocation ratio for all share classes

Funds of funds

A simplification rule for funds of funds is already in place. At Level 1, the asset source of target funds is classified according to the fund categories set out in the BMF Circular on the Investment Tax Act (text no. 66) dated 18 August 2009.

At Level 2, funds of funds can make use of another simplification rule for the allocation between current income and other realised gains/losses from the disposal of investments.

Transitional rules for cost allocation

There are transitional rules in place to allow for a less than strict interpretation. The BMF will accept a different general expense allocation for fiscal years beginning before 1 April 2015 and will not request retroactive corrections.

Investment restrictions *(Anlagebestimmungen)* and asset classification

Requirements within investment restrictions

The InvStG establishes its own scope of application, apart from the investment law (KAGB). UCITS and AIFs are considered to be investment funds if they fulfil the requirements of e.g. supervision, right of redemption, risk diversification and no active commercial management of the assets.

- A temporary suspension of fund unit redemption for up to 60 months is accepted, e.g. for the winding up of portfolios
- The fiscal authority will consider foreign UCITS as being risk diversified without assessment. A temporary mismatch at launch/winding up is accepted

Inadequate asset classification by a data vendor

If a data vendor (e.g. WM Datenservice) provides an inadequate asset classification for a German tax reporting calculation, a correction has to be made when this is brought to light. Future publications under section 5 of the InvStG must also reflect the correction.

A temporary suspension of fund unit redemption for up to 60 months is accepted, e.g. for the winding up of portfolios

Lump-sum taxation under section 6 of the InvStG

German lump-sum taxation rules breach the EU principle of free movement of capital, according to the 'Van Caster' decision of the European Court of Justice (C-326/12).

In general, funds have to fulfil German tax reporting requirements (calculation and publication) for German investors within four months after the end of the fiscal year or, if applicable, after a formal distribution resolution. If such tax-relevant information has not been made available or the related publication requirements have not been met, the taxable income attributed to German investors through investments in "non-transparent investment funds" has to be determined on a lump-sum basis (a minimum of 6% of NAV at the end of the calendar year).

The ECJ decision

In its decision C-326/12 dated 9 October 2014, the ECJ ruled that lump-sum taxation under the German investment fund tax reporting regime breaches the EU concept of free movement of capital, as investors are not allowed to provide tax authorities with proof of actual income generated using appropriate documents or information.

Following this ECJ decision, the BMF issued a draft circular dated 31 October 2014 giving guidance on how to provide the tax authorities with proof of actual income generated through appropriate reporting. The level of detail and depth has to be the same as in the relevant fiscal year-end publication in the Federal Gazette (*Bundesanzeiger*). Only the strict timeline (four months after the fiscal year-end or formal distribution resolution within four months) can be omitted.

Future approach: non-transparency?

There are current discussions about a completely new approach with respect to the taxation of mutual funds. This future approach might include a tax regime for mutual funds without any reporting requirements. The specific outcome is still unknown.

In general, funds have to fulfil German tax reporting requirements for German investors

India

The regulatory and tax framework for offshore funds investing in India

Rajesh H. Gandhi
Partner
Deloitte

Karamjeet Singh
Senior Manager
Deloitte

India opened its capital markets to Foreign Institutional Investors in 1992 as a part of wider economic reforms. Foreign Institutional Investors or FIIs (as they are popularly known in India) have played a very important role in the growth of the country's economy as well as its capital markets. FII investments have grown (on a net basis) from US$826 million in 1993 to US$39 billion in 2014 (January to November 2014). Cumulative net investment by FIIs since 1992 has totalled over US$200 billion (www.sebi.gov.in).

Prior to investing in India, the first step is to seek a licence or registration from the capital market regulator, the Securities and Exchange Board of India (SEBI). Since January 2014, the SEBI has overhauled the regulations applicable to FIIs and replaced the earlier FII regulations with the new foreign portfolio investor (FPI) regulations.

Prior to investing in India, the first step is to seek a licence or registration from the capital market regulator, the Securities and Exchange Board of India (SEBI)

Under the new regulations, any foreign investor (subject to meeting entry conditions) can invest in the Indian capital markets. This is a significant relaxation from earlier norms, where only specific types of investor (such as sovereign funds, pension funds, mutual funds, etc.) were eligible to register as FIIs or sub-accounts. For instance, non-broad based funds, family offices, foreign corporates or individuals who could not get registration under the earlier regime can now register as Category III FPIs. Furthermore, in the new regulations, there is no requirement for non-fund investors such as banks or insurance companies to introduce a broad based sub-account (with 20 or more investors) as in the earlier regime.

The other significant change made by the new regulations is that the SEBI has now delegated the process of granting registrations to the sub-custodians, which are called Designated Depository Participants (DDPs). Also, an outer timeline of 30 days has been set by the SEBI for custodians to grant registrations to FPIs. On the flip side, the Participatory Note (P-Note) regime has been made very strict and only regulated funds eligible to invest as FPIs will now be allowed to subscribe to P-Notes of FPIs. Moreover, investments under the P-Note route and FPI route will be pooled for the purposes of monitoring the investment ceiling. This will require FPIs issuing P-Notes to have a more robust KYC and investment monitoring framework. In addition, FPIs are no longer allowed to invest in unlisted shares.

An overview of the regulatory and tax framework applicable to FPIs is provided on the following pages.

FPI regulations

Definition of FPI

The regulations define a Foreign Portfolio Investor (FPI) as a person who satisfies the eligibility criteria prescribed under the regulations and has been registered as an FPI. Existing FIIs, sub-accounts and Qualified Foreign Investors (QFIs) have been grandfathered as FPIs.

Conditions to be met by an investor to register as FPI:

- The investor is not resident in India and is not a non-resident Indian
- The investor is a resident of a country whose securities market regulator is a signatory to the IOSCO (International Organization of Securities Commissions) Multilateral Memorandum of Understanding (Appendix A Signatories) or a signatory to a bilateral memorandum of understanding with the SEBI
- If the investor is a bank, it should be resident in a country whose central bank is a member of the Bank for International Settlements
- The investor is not resident in a country identified in the Public Statement of the Financial Action Task Force
- The investor entity should not be an opaque structure such as a protected cell company, segregated cell company or equivalent, where the details of the ultimate beneficial owners are not accessible/ring fenced, etc.
- The investor is legally permitted to invest in securities outside its own country and is authorised by its memorandum of association or articles of association or equivalent document to invest on its own behalf or on behalf of clients
- The investor has sufficient experience, a good track record, is professionally competent, financially sound and has a good reputation of fairness and integrity

For its part, the Indian government has tried to contribute by easing the regulatory framework for FPIs

FPI categories

The following three categories have been prescribed in the regulations under which FPIs would be registered. The categories are based on the risk profile of investors, with Category I being the lowest risk category. The KYC documents required from an investor have been rationalised on the basis of the category to which it belongs.

Category I	Category II	Category III
Government and government agencies	*Broad based funds including mutual funds, investment trusts, insurance/reinsurance companies	Non-broad based funds, unregulated funds
Central banks	*Banks, asset management companies, investment managers/ advisors, portfolio managers	Corporate bodies, trusts, individuals, family offices
Sovereign wealth funds	University funds, pension funds	Endowments, charitable associations/trusts/foundations
International or multilateral organisations/agencies	University-related endowments registered with the SEBI as FIIs/ sub-accounts	Other foreign investors not covered in Category I & II

*The entity needs to be regulated by the securities market regulator or banking regulator. In the case of an unregulated broad based fund, its investment manager should be appropriately regulated and registered as an FPI, and remain accountable for the fund's compliance.

Key investment conditions and restrictions

The key investment conditions and restrictions are listed below:

- Investments are permitted in equity shares, preference shares, government bonds, corporate bonds, mutual fund units, warrants, exchange traded derivatives, commercial papers, Indian depository receipts, security receipts of asset reconstruction companies
- Investment in shares, bonds (other than in the infrastructure sector), warrants restricted to *"listed"* or *"to be listed"* securities
- Investments in equity shares by a single FPI or an investor group (i.e. multiple FPIs with common beneficial owners) must amount to less than 10% of the issued capital of the company
- Investment in bonds is subject to the availability of debt limits
- Investments in exchange traded derivatives are subject to the position limits and margins stipulated by stock exchanges
- Investment in equity shares subject to margins stipulated by stock exchanges
- Securities can be purchased either from the issuer in the primary market or through a registered broker in the secondary market
- Category I & II FPIs (except for unregulated broad based funds) can issue offshore derivative instruments (such as participatory notes) on the basis of underlying Indian securities to regulated entities eligible for FPI registration in India
- Investment in the equities of an Indian company by all FPIs taken together is restricted to 24% of the paid-up capital or the limit approved by the company by special resolution (subject to a sector cap/statutory limit)
- Investments are not permitted in companies engaged in the defence industry (subject to licensing requirements), chit funds, Nidhi companies, agricultural or plantation activities, real estate or the construction of farm houses or trading in Transferable Development Rights (TDRs)
- The currency risk on the market value of investment in equities and debt securities can be hedged by executing forward instruments and options contracts. IPO-related flows can be hedged using FCY-INR swaps
- Investment in the equity shares of private sector banks by FPIs is restricted to 5% of the paid-up capital
- Sale proceeds or any other income can be remitted out of India only after payment of taxes

Tax framework

Tax rates

Typically, income earned by FPIs in India includes gains from the sale/transfer of securities, dividends and interest. The domestic tax rates applicable to FPIs are discussed below.

Capital gains: capital gains are divided into long-term and short-term capital gains. In the case of listed securities and units of equity-oriented mutual funds, if the security is held for more than one year, it results in long-term capital gains, and if sold within a year, it results in short-term capital gains. For other securities (including unlisted securities), this threshold period is three years. Long-term capital gains earned from the sale of equities on the stock markets and from the sale/redemption of units of equity- oriented mutual funds are exempt from tax, whereas short-term capital gains from such transactions are taxed at 15%. The capital gains earned from other transactions (including bonds, derivatives or the off-market sale of equity shares) are taxed at 10% for long-term gains and 30% for short-term gains.

Under the new regulations, any foreign investor (subject to meeting entry conditions) can invest in the Indian capital markets

Dividends: dividends received by FPIs from Indian companies are exempt from tax, as the Indian company is required to pay a dividend distribution tax of 15% on them. Dividends paid by foreign companies in India on Indian depository receipts are taxable at 20%.

Interest: until May 2015, interest income earned from government securities and most corporate bonds is taxable at 5%. If the current concessional tax rate is not continued, interest income will be taxable at 20% after May 2015.

The tax rates mentioned above are as per the domestic tax law and required to be increased by a surcharge and education cess (rate), which depends on the quantum of income and legal status of the taxpayer. If the FPI is a tax resident of a country with which India has entered into a tax treaty, the treaty provisions would be applicable to the extent that they are more beneficial to the FPI. For instance, in case of funds based in Mauritius, Singapore or even certain European countries such as Belgium, Denmark, France etc., capital gains earned in India are not taxable provided the treaty conditions are met.

FPIs that route their investments through tax-efficient countries such as Mauritius are concerned about the proposed implementation of General Anti-Avoidance Rules (GAAR)

Recent developments

Clarification of the treatment of income from the transfer of securities: in the 2014 Budget, the Indian government clarified that the income earned by FPIs from the transfer of securities would be classified as capital gains. This clarification has put to rest the controversy on whether to treat such income as capital gains or business income. Moreover, it was also mentioned that this clarification should encourage FPIs to locate their fund managers in India, as there should be no concerns regarding the location of the fund manager in India being taxed as a permanent establishment of the FPI.

GAAR: FPIs that route their investments through tax-efficient countries such as Mauritius are concerned about the proposed implementation of General Anti-Avoidance Rules (GAAR) likely to be enacted from April 2015. Under the GAAR, the tax authority will have the power to tax any arrangement that lacks commercial substance or where the main purpose of the arrangement is to avoid tax or to misuse/abuse the provisions of the law.

Taxpayers are concerned that various structures could be challenged on the argument that they are abusive. This concern emanates from the fact that there are no objective tests provided in the law to test the various triggers mentioned in the GAAR, such as the lack of commercial substance or misuse/abuse of the law, and therefore the ground level tax officer may take an aggressive stance—especially in the case of investments through tax-efficient countries such as Mauritius. There is an expectation that the government will issue certain clarifications or may even defer the enactment of the GAAR, but any official announcement in this respect is expected only in February 2014 when the Finance Minister presents the Budget for 2015. Fortunately, GAAR will not apply to FPIs where the annual tax benefit does not exceed approximately US$500,000.

Indian tax implications for the transfer of shares of entities located outside India: in 2012, the Indian government amended the income tax law with retrospective effect from 1962 to clarify that the transfer of shares or interests in a foreign entity would be taxable in India if such entity derives substantial value from assets located in India.

The Indian government clarified that the income earned by FPIs from the transfer of securities would be classified as capital gains

While these provisions have not been enforced on investments under the FPI route, technically, the transfer of shares/interests by the beneficiaries of the funds as well as the restructuring of the funds could be subject to tax in India, especially in the case of India-focused funds.

There have been multiple representations on this aspect by investor forums to the Indian government to keep stock market investments outside the scope of indirect transfer tax, but there has been no clarification from the government on this issue as yet.

India is now on the world stage in relation to fund investments, and the Indian stock market has been one of the best performers globally this year. For its part, the Indian government has tried to contribute by easing the regulatory framework for FPIs. While FPIs enjoy a simplified tax regime, recent changes such as the GAAR and indirect share transfers are being watched carefully by foreign investors. Any clarifications on these aspects for FPIs will certainly be welcome.

Ireland

Deirdre Power
Partner
Financial Services Tax
Deloitte

Kelly O'Brien
Manager
Financial Services Tax
Deloitte

ICAV

The Irish Collective Investment-management Vehicle (ICAV) will be Ireland's newest corporate fund vehicle. The ICAV offers enhanced distribution and a simplified compliance model. The ICAV is being introduced under new legislation which is tailor-made for investment funds resulting in a more efficient and effective fund structure.

The ICAV has many benefits over the existing fund structures available in Ireland. The aim of the ICAV is to combine the advantages of each of the existing fund vehicles into one, offering many benefits to investors and promoters.

The ICAV offers an attractive alternative fund structure, both for existing funds who may opt to convert to an ICAV and also for new funds being established

The main advantages of the ICAV include:

- Future proofing against company law changes in Ireland and in Europe
- U.S. *"check the box"* election is possible (the existing Variable Capital Company (VCC) structure is not eligible for *"check the box"*)
- Can hold a single asset
- The ability to prepare financial statements on a sub-fund basis
- Easier to amend constitutional documents
- The ability to elect to dispense with an AGM

The ICAV is optional, so existing structures are not obliged to change, but have the option to do so if they wish. We would expect that funds may decide to change to the ICAV where the cost-benefit of changing is favourable.

Existing VCCs will be in a position to convert to an ICAV through a simplified conversion process. Overseas investment companies will be able to convert to an ICAV under the streamlined re-domiciliation migration one-step process introduced in 2009, rather than being required to migrate and then convert.

Conversion and migration will be available to both UCITS and AIFs structured as corporate entities.

Under the current draft of the legislation, UCITS can merge to form ICAVs, but it remains to be seen whether AIFs will be permitted the same flexibility. It is envisaged that mergers of existing overseas funds will be through a streamlined one-step approach process.

When considering if you should convert your existing VCC into an ICAV, the tax matters to be addressed include:

- Have your US tax advisors reviewed your proposed ICAV structure to ensure that any sub-funds are suitable for *"check the box"* election and meet your US tax objectives?
- Will *"checking the box"* trigger any adverse tax consequences for US investors who currently treat the investment as opaque?
- Liaise with your tax advisors on foreign tax reporting to understand if any considerations need to be addressed (e.g. German, UK, Swiss tax reporting).
- Is the same Investment Undertaking Tax (IUT) number still appropriate?
- Will the non-residency fund tax declarations remain intact for the new ICAV (as the forms are in the name of the VCC)?
- Will the nature of the changes give rise to any unintended disposal or other tax implications for existing investors?
- Is the service provider able to perform the required reporting for US investors if the *"check the box"* option is utilised?

From an Irish tax perspective, the ICAV falls within the normal funds tax regime, i.e. gross roll up fund, which pays no direct tax in Ireland when all investors are non-Irish resident.

The ICAV offers an attractive alternative fund structure, both for existing funds who may opt to convert to an ICAV and also for new funds being established.

AIFM

Irish tax legislation has been updated to confirm that an Alternative Investment Fund (AIF) managed by an Irish Alternative Investment Fund Manager (AIFM) will not fall within the Irish tax net, purely by virtue of its being managed by an Irish AIFM. This confirmation is very welcome for the Irish funds industry, given that many global investment managers have chosen Ireland as the location for their AIFM. This Finance Act change gives comfort that the AIFs managed by such AIFMs will not automatically fall within the Irish tax net.

Change to employment taxes that benefit the funds industry

A number of changes to the personal tax system in Ireland may encourage more senior executives with industry expertise to relocate to Ireland.

The higher rate of personal income tax in Ireland has dropped by 1% to 40%.

Ireland has put in place a Special Assignee Relief Programme (SARP) which has been enhanced in the recent Finance Act. The SARP programme has been extended to continue for another number of years, the upper salary limit has been removed, the residency requirement has been amended and the exclusion from working abroad has been removed. In addition, an assignee is only required to have been employed abroad by the employer for a reduced period of 6 months going forward in order to be in a position to obtain the relief.

Another relief, which is the foreign earnings deduction, has also been enhanced with the potential to benefit employees who work abroad on a regular basis. The maximum deduction per annum is €35,000, the number of days working abroad has been reduced to 40 (previously 60), the number of consecutive days abroad per trip has been reduced to 3 (previously 4), time travelling between countries is now included in calculating days abroad and the number of qualifying states has been extended. All in all, this could benefit employees of the funds industry who undertake work abroad on a regular basis.

Exchange of information

The Finance Act has introduced provisions for the collection and reporting of information with regard to financial accounts held by a person who is tax resident in another country.

This is in anticipation of the introduction of the Common Reporting Standard following the Multilateral Competent Authority Agreement recently signed by more than 50 jurisdictions (including Ireland), which will allow for the implementation of the OECD Automatic Exchange of Information Standard.

Additional regulations may be introduced outlining further detail on the reporting obligations. Any common reporting standards introduced in Ireland (and indeed globally) are likely to impact the funds industry.

New tax treaties

Ireland continues to expand its network of double taxation treaties, 72 of which have now been signed. The legal procedures to bring our most recent treaties into force—treaties with Ukraine, Thailand, Botswana and Ethiopia – are now being followed. In addition, negotiations for new agreements with other jurisdictions are ongoing.

The ever-increasing number of Irish treaties serves to improve returns for investors in Irish funds, with Irish funds recognising the benefit of reduced rates of foreign tax in treaty countries in many cases.

Common Contractual Fund (CCF)

The Common Contractual fund (CCF) is an Irish regulated asset pooling fund structure. Asset pooling enables institutional investors to pool assets into a single vehicle fund with the aim of achieving cost savings, enhanced returns and operational efficiency through economies of scale. Experience of existing CCFs shows a saving of 10-20 basis points.

A CCF is an unincorporated body established under a deed whereby investors are 'co-owners' of underlying assets that are held pro rata to their investment. A CCF is usually established by a management company and investors must not be individuals, i.e. only institutional investors are permitted. CCFs are authorised and regulated by the Central Bank of Ireland and can be structured as a UCITS or a non-UCITS fund. A CCF is not a separate legal entity and is transparent for Irish legal and tax purposes.

As the CCF is fiscally transparent, it is therefore exempt from Irish tax on its income and gains. Investors in a CCF are treated as if they directly own a proportionate share of the underlying investments of the CCF.

Key benefits of the CCF are:

- Well established with a proven track record
- More than 70 CCFs in operation, both UCITS and non-UCITS
- Wide investor base – institutional investors, pension funds, insurance companies, corporates, life assurance companies, asset managers and MNCs
- Purpose built for the funds industry
- Tax transparency in at least 20 countries
- Transparency enshrined in many of our double taxation agreements
- Can lead to tax savings of approximately 20bps, depending on the investor/investment mix
- Experienced services providers in the industry

Real Estate Investment Trusts (REIT)

Since its launch in 2013, the Irish REIT offers investors a way to invest in the Irish property market in an efficient tax manner. The key benefits of the REIT include:

- Tax exemption in respect of the income and chargeable gains of a property rental business held within a company
- Access to Ireland's extensive treaty network (see above)
- Capital gains made by non-Irish resident investors on their disposal of shares in a REIT are not taxable in Ireland

To date three REITs (Green REIT Plc, Hibernia REIT plc and IRES REIT) have been established and have managed to raise circa €1.27 billion. We expect to see further REITs in 2015 with expansion beyond Irish investments to include foreign property.

2015 promises to be an interesting year for the Irish funds industry, particularly with the positive developments like the ICAV coming into play

Netherlands

Ernst-Jan Nolta
Senior Manager
Financial Services Tax
Deloitte

Raymond Adema
Manager
Financial Services Tax
Deloitte

The debate over the levying of Dutch dividend withholding taxes has continued over the last year, and there are a number of cases pending. Below, we cover some of the cases of interest to the asset management industry.

Withholding tax reclaim opportunities

Investment companies and investment funds

Just before the end of 2013, the Dutch Supreme Court issued its judgement in the Finnish Investment Fund case.

The court judged that the Netherlands is not obliged to follow the tax rules (i.e. tax exemptions in this case) of another member state. Instead, the test should be how the entity would be taxed in the Netherlands. Therefore, despite being tax exempt in Finland, the Finnish open-ended investment fund would be subject to tax if resident in the Netherlands. As such, the company could not benefit from the reimbursement of Dutch dividend withholding tax.

The investment fund argued that it should be seen to be the Finnish equivalent of a Dutch Fiscal Investment Institution (FII) and would therefore be subject to a 0% tax rate in the Netherlands. However, as the Finnish investment fund did not actually distribute its income as dividends to its shareholders, the Dutch Supreme Court did not consider the entity to be comparable to a Dutch FII. It did not, however, discuss the application of this condition in more detail, and did not explain any of the other conditions that need to be fulfilled by foreign investment companies and investment funds in order to be considered comparable to an FII (comparability test) and be entitled to a refund of Dutch dividend withholding tax. As a result, several cases are pending before the Dutch courts in order to clarify the conditions for the comparability test.

Finally, it remains somewhat disappointing that the Dutch Supreme Court did not put any preliminary questions to the European Court of Justice, even while similar cases were pending, such as the Emerging Market Series case and an infringement procedure against Denmark.

Life insurance companies

Last year, the European Commission started an infringement procedure against the Netherlands, because of the discriminatory taxation of dividends received on shares held by insurance companies established in another member state or in an EEA country (Norway, Lichtenstein and Iceland).

Under Dutch law, Dutch insurance companies are not taxed on dividends received on shares held in accordance with the unit-linked insurance framework. For such companies, the dividend withholding tax is an advance payment in respect of corporate income tax, which is levied on a net basis. As a result, Dutch insurance companies are able to deduct the increase of the obligation to pass the dividends on to their policyholders against the dividends received. Therefore, the corporate income tax base is effectively reduced to (close to) zero, while any Dutch dividend withholding tax may be credited against the corporate income tax liability, or refunded if it exceeds the corporate income tax liability.

The Dutch dividend withholding tax is a final taxation for insurance companies established in the EU or the EEA receiving Dutch dividends on shares held in the framework of unit-linked insurance. Unlike Dutch insurance companies, they are taxed on gross dividends, and cannot obtain a corresponding tax credit.
The European Commission considers the higher taxation of insurance companies established elsewhere in the EU/EEA to be incompatible with the freedom of capital movement within the meaning of the Treaty on the Functioning of the European Union and the European Economic Area (EEA) Agreement.

Other (non-life insurance) companies

The debate over the levying of dividend withholding tax is not limited to investment companies, investment funds and life insurance companies. In another Dutch case (*Société Générale*), the CJEU was asked by the Dutch Supreme Court to clarify the standard of comparability when assessing a dividend withholding tax violation. The specific question is whether a settlement of dividend withholding tax as an advance payment in respect of the corporate income tax due in domestic situations by the entity receiving a dividend—while such settlement is not possible for a foreign entity receiving a dividend—constitutes a breach of EU law.

The uncertainty over the levying of Dutch dividend withholding tax is expected to continue in 2015

Switzerland

New tax opportunity for investment funds

André Kuhn
Senior Manager
Financial Services Tax
Deloitte

Danielle Koyuncu
Manager
Financial Services Tax
Deloitte

Aberdeen withholding tax claims

Dividend payments received by Swiss investment funds on stocks from companies domiciled in a European Union (EU) member state could be subject to domestic withholding tax levied on outbound dividends. Under an applicable double tax treaty, such withholding tax may typically be reduced to 15% for portfolio investments. However, the tax treatment of dividends paid to resident investment funds and comparable non-resident investment funds may differ, and may therefore result in discriminatory treatment.

In 2009, the European Court of Justice (ECJ) reached a decision in the Aberdeen case (C-303/07), ruling for the first time that levying withholding tax on dividends paid to non-resident investment funds is discriminatory if the same dividends paid to resident investment funds are exempt from withholding tax. In the Aberdeen case, a Finnish resident real estate company, Aberdeen Property Fininvest Alpha Oy (Aberdeen), which was owned by a real estate fund incorporated as a Luxembourg SICAV, asked the Finnish tax authority whether dividends distributed to the Luxembourg SICAV could be exempt from Finnish withholding tax. Aberdeen considered such taxation to be discriminatory under EU law, because the same dividend payments to a Finnish corporation or investment fund would have been exempt from withholding tax.

As the Finnish tax authority rejected the exemption, Aberdeen submitted the issue to the Finnish courts, which referred the matter to the ECJ. The ECJ resolved that the different tax treatment of non-resident and resident investment funds represents a restriction to the freedom of establishment and the free movement of capital principles.

Since then, the ECJ has confirmed in new court cases that discriminatory tax regimes contravene EU law. In particular, the ECJ explicitly stated in the Santander case (C-338/11 to C347/11) in May 2012 that the French tax treatment of dividend payments to non-resident investment funds was contrary to the free movement of capital principle and is not compatible with EU law. As the free movement of capital principle is also applicable to non-EU countries, this decision is applicable to both EU and non-EU resident investment vehicles, including mutual investment funds. Furthermore, the ECJ stated that the decision has retroactive effect, thereby allowing investment funds to claim back discriminatory withholding tax for past years.

Lastly, in April 2014, the ECJ decided in the EMS DFA Case (C-190/12) that Poland's tax treatment of outbound dividends to a U.S. investment fund was contrary to the free movement of capital principle and allowed the U.S. investment fund to recover withholding tax incurred in Poland.

The Polish authorities claimed that the withholding tax treatment should not be assessed under the free movement of capital principle, but under the principles of freedom of establishment or freedom to provide services instead. As the freedom of establishment and the freedom to provide services principles are only applicable to countries that are a member of the EU or the European Economic Area (EEA), this would have excluded investment funds in third countries such as Switzerland from recovering discriminatory withholding tax.

However, the ECJ decided that for portfolio investments, the Polish tax treatment was contrary to the free movement of capital principle, which finally opened the door for third country investment funds (such as Swiss investment funds) to claim back discriminatory withholding tax levied in EU member states.

Based on these ECJ decisions, and in view of the tax laws of EU member states, there might be opportunities for Swiss investment funds to reclaim discriminatory withholding tax incurred in Austria, Belgium, Denmark, Finland, France, Germany, Italy, the Netherlands, Norway, Poland, Spain and Sweden.

We therefore recommend that Swiss investment funds and investment foundations review their past withholding tax positions, and consider whether it would be beneficial to reclaim discriminatory withholding tax.