AG Opinion regarding Netherlands' withholding tax on dividends paid to foreign investment funds

Netherlands – Withholding Tax on Dividends – Investment Fund – Free Movement of Capital – Fidelity Funds

On September 5, 2019, Advocate General (AG) Pitruzzella of the Court of Justice of the European Union (CJEU) rendered his opinion in the Köln-Aktienfonds Deka case (C-156/17) concerning the compatibility with EU law of the Dutch withholding tax on dividends distributed to non-resident investment funds. The AG concluded that the shareholders and distribution requirements imposed by the Dutch legislation to benefit from a tax refund may be contrary to the free movement of capital.

Background

Köln-Aktienfonds Deka is a contractual investment fund established in Germany, which is compliant with the requirements of the EU Directive 2009/65/EC on Undertakings for Collective Investment in Transferable Securities (UCITS). Köln-Aktienfonds Deka had portfolio investments in the Netherlands that did not exceed 10% of the share capital of the participations held. The UCITS claimed the repayment of the withholding tax levied on dividends received from Dutch companies between 2002 and 2008, based on EU law.

Under Dutch tax law, dividend distributions to both resident and non-resident investment funds are subject to a 15% withholding tax. However, Dutch funds that elect to be treated as a "Fiscal Investment Institution" ("FII") are entitled to a tax credit that is offset against the dividend withholding tax they levy when they further distribute profits to their unitholders. As a consequence, the Dutch dividend withholding tax is effectively being refunded to Dutch FIIs that meet a distribution and certain shareholders requirements. On the contrary, the Dutch withholding tax on dividend distributions constitutes a final tax burden for foreign investment funds, as they are not entitled to any tax credit upon distribution of their profits. Köln-Aktienfonds Deka argued that this different treatment is contrary to the free movement of capital and requested a refund of the tax levied.

On March 27, 2017, the Dutch Supreme Court decided to refer to the CJEU the question whether the Dutch withholding tax is in line with the free movement of capital. As a result of the subsequent CJEU ruling in the Fidelity Funds case (C-480/16), the questions were further amended in December 2018 to focus on whether the shareholders and distribution requirements are in line with EU law.

The AG Opinion

Addressing first the requirements imposed by the Dutch legislation as regards the shareholders of qualifying FIIs, the AG noted that both resident and non-resident investment funds are subject to the same conditions. However, non-resident taxpayers requesting the benefit of a tax advantage should not be subject to an excessive administrative burden, such that it is in fact impossible for them to qualify for the benefit. In that respect, any difficulty that the non-resident taxpayers may have in providing supporting evidence that they fulfill the applicable requirements is not a problem for which the Netherlands should have to answer. The AG further added that data privacy rules applicable within the EU are not such as to limit the right of the investment funds to provide relevant data on their shareholders to the Dutch tax authorities. However, if the latter only request such information from non-resident qualifying funds and not from Dutch FIIs, such practice could be contrary to EU law. The AG concluded that it is for the referring court to assess whether this is effectively the case. Finally, the AG confirmed that it should also be for the Dutch Supreme Court to check whether the listing requirement applicable until 2007 constitutes a discrimination.

As regards the obligation for qualifying investment funds to distribute their profits within eight months as of the end of the corresponding financial year, the AG observed that denying the benefit of the FII regime to a non-resident fund whose profits are subject to tax in its state of residence, irrespective of whether such profits have been distributed or not, could constitute a restriction on the free movement of capital. This is particularly the case if it is impossible or excessively difficult for this non-resident fund to comply with the Dutch distribution requirement. In that regard, the AG recalled that the situations of a resident and a non-resident fund are comparable in light of the objective of the Dutch regime to ensure tax neutrality between direct and indirect investments in Dutch securities. Referring to the CJEU's decision in the Fidelity case, he further concluded that the Dutch tax authorities should take into account the tax paid by Köln-Aktienfonds Deka to the German tax authorities when assessing whether the investment fund is entitled to a refund of the Dutch withholding tax. Finally, the AG successively considered and rejected possible justifications based on the need to ensure a balanced allocation of taxing rights and the need to safeguard the coherence of the Dutch tax system. With regard to the latter, he recalled that a less restrictive measure would be to allow non-resident UCITS to benefit from the withholding tax exemption, provided they pay a tax equivalent to that which Dutch FIIs are liable to levy on profit distributions to their investors. Consequently, the AG concluded that the Dutch legislation is contrary to the free movement of capital in cases where if it is impossible or excessively difficult for a non-resident fund to comply with the Dutch distribution requirement, and the fund's profits are subject to tax in its state of residence, irrespective of whether they have effectively been distributed.

EU Tax Centre comment

Although it remains to be seen whether the CJEU will follow this opinion, AG Pitruzzella provides much needed clarity on a number of issues that the CJEU had left unanswered in its

decision in the Fidelity Funds case (June 21, 2018, C-480/16). In particular, the AG confirms that in his view a less restrictive measure would be for the Dutch tax authorities to assess whether the German tax paid by Köln-Aktienfonds Deka upon an effective or deemed profit distribution to its shareholder could be considered as a tax equivalent to that which it would be liable to levy in the Netherlands, would the fund be resident there. In other words, if the German investment fund has paid German (withholding) tax that is at least equal to the Dutch dividend withholding tax, the Netherlands must accept this. The AG also provides some interesting insights into the compatibility with EU regulations on data privacy of providing shareholders' personal data to tax authorities, when requesting a withholding tax refund.

Should you have any queries, please do not hesitate to contact KPMG's EU Tax Centre, or, as appropriate, your local KPMG tax advisor.

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