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AG opinion in the joined cases Miljoen, X, and Société Générale

Free movement of capital – net taxation – withholding tax on dividends – individual portfolio investor – corporate portfolio investor

On June 25, 2015, Advocate General (AG) Jääskinen of the Court of Justice of the European Union (CJEU) gave his opinion in the joined cases Miljoen (C-10/14), X (14/14) and Société Générale (C-17/14). The AG concluded that withholding tax imposed on a non-resident may not exceed the individual income tax burden of a resident taxpayer. In addition, a discrimination in the source state can only be neutralized by a tax credit in the state of residence, if the possibility of a full tax credit exists in the state of residence.

Background

The cases concern the Dutch tax treatment of dividends received by non-resident portfolio investors, and the question whether – and which elements of – income taxation should be taken into account when assessing the compatibility with the free movement of capital of the Dutch 15% withholding tax (WHT) levied on dividends distributed to non-residents :

– Mr. Miljoen is a Dutch national resident in Belgium, who incurred a final 15% WHT on dividends received from Dutch companies. Mr. Miljoen claimed a refund for the part of the Dutch WHT exceeding

the income tax he would have paid, had he been resident in the Netherlands and taxed under the so-called Box 3 regime.
- Mrs. X is in a similar situation to Mr. Miljoen. In addition, she was subject to a 25% income tax in Belgium on the net dividends received. Although the 15% Dutch WHT was deductible for Belgian income tax purposes, Belgium denied Mrs. X the possibility of crediting the latter on her Belgium income tax, as foreseen by the relevant double tax treaty (DTT).
- Société Générale S.A. is a French resident company. The company had the possibility to credit the Dutch WHT on its French corporate income tax, but could not fully benefit from the tax credit because of losses incurred in France. In addition, Société Générale S.A. incurred direct (e.g. interest on financing of the shares) and indirect (e.g. hedging) costs in relation to its investments, which were not taken into account in the Netherlands, since the Dutch WHT is levied on the gross income distributed.

The Dutch Supreme Court referred several questions to the CJEU. First the Court observed that a 15% Dutch WHT is levied on dividends distributed to portfolio investors, irrespective of their place of residence. However, resident taxpayers may credit the WHT suffered on their income tax due, while the WHT is a final tax burden for non-residents. As a consequence, the question arose in all cases whether or not Dutch (corporate or individual) income tax should be taken into account when assessing the comparability of a resident and a non-resident taxpayer.

In addition, the Court sought guidance from the CJEU as to which elements should be considered when comparing the effective tax burdens of resident and non-resident investors.

Finally, both in the X case and in the Société Générale case, the Court asked additional questions regarding the effect of a potential neutralization by way of a DTT or of a unilateral national measure, should the CJEU conclude to the existence of an effective discrimination.

The AG's opinion

In all three cases the AG is of the opinion that the Dutch dividend WHT is fully creditable (without any limitations) with the individual and corporate income tax if the recipient is a resident of the Netherlands. Therefore, the Dutch WHT is in other words actually always refunded and replaced by an individual or corporate income tax. For a non-resident the Dutch WHT is a final levy. When comparing a resident and a non-resident shareholder, the comparison should not only be restricted to the Dutch WHT, but should also include the income tax to which the WHT is an advance levy.

In calculating the effective individual income tax burden for a resident, the statutory deemed income of 4% should be applied on all shares for the tax year concerned where loans used to purchase the shares are deductible. In addition, the tax free amount that is granted to residents should be included in the calculation as well. The outcome of this calculation should be multiplied by the flat 30% tax rate and be compared with the 15% Dutch WHT that a non-resident individual

shareholder has paid. If the Dutch WHT is higher, then the non-resident is eligible for a tax refund of the difference.

For the comparison of the non-resident and resident company, the Dutch WHT should be compared with the corporate income tax that a resident company would have paid on net dividend income where the cost of financing, transaction and holding of the share are deductible. The gain or loss on the sale of the shares should not be included in the comparison. The AG leaves however for the national court to decide whether the arbitrage related costs such as losses on other shares than those from which the dividends were derived should be taken into account.

With respect to the question whether the discrimination in the source state can be neutralized by a tax credit in the state of residence, the AG is of the opinion that if it is clear that the state of residence has, in the past, provided for this neutralization (by providing a tax credit for the Dutch WHT paid), the source state no longer needs to eliminate the discrimination. However, the AG also argues that the DTT between the source state and the state of residence should provide for a full tax credit without limitation, to eliminate future potential discrimination for investors. The possible foreign tax credit carryover provided for in a DTT is only acceptable in the event that the result is comparable to the treatment of a resident shareholder. This requirement will not be met if a resident shareholder would always receive a full credit or refund without the need to carry over to future years and the carryover for a non-resident shareholder would not guarantee the utilization of such a carryover (for example, in the case of ongoing losses).

EU Tax Centre Comment

The AG has once again confirmed that in a case where a resident taxpayer can fully credit a WHT imposed against income tax, non-residents may not be subject to a higher effective income tax burden than residents. In addition, tax treaties should provide for the possibility of a full tax credit. A tax credit carryover is only acceptable if a resident shareholder is given the same treatment.

Should you require further assistance in this matter, please contact the EU Tax Centre or, as appropriate, your local KPMG tax advisor.

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