

## Investment Management

# Pension Funds can claim back WHT in Europe – Latest developments

In December 2005, PricewaterhouseCoopers' EU Direct Tax Group (EUDTG) and the European Federation for Retirement Provision (EFRP) jointly lodged complaints with the European Commission against 18 EU Member States for their discriminatory taxation of dividend and interest payments to foreign EU pension funds. The Commission agreed with this analysis and has started infringement proceedings against most of these Member States since May 2007. Recent judgments of the European Court of Justice (ECJ) support the Commission's action. Today, 4 years later, we are finally beginning to see the first results of the groundbreaking initiative of PwC and EFRP with the first refunds being granted by the Dutch and Austrian tax authorities and promising developments in France and Spain, and other countries as well.

### BACKGROUND

In 2005, a study by PwC found that 18 EU countries exempt domestic pension funds from paying corporation and/or income tax and usually also withholding tax on dividend and interest. In the case no withholding tax exemption at source is available, domestic funds normally have access to a refund procedure. However, foreign pension funds can either not qualify for the relief at source or are denied access to the refund procedure. As a result, non-resident pension funds pay higher taxes on interest or dividends than resident pension funds. This dissuades foreign pension funds from investing in other Member States and domestic companies in attracting capital from foreign pension funds.

According to the Commission, this situation breaches Community Law, in particular Article 56 of the EC Treaty, the free movement of capital within the EU. Recent ECJ judgments support the view of the Commission. The *Denkavit* Case for instance confirmed that outbound dividends must not be subject to higher taxation in the source State than domestic dividends.

### LATEST DEVELOPMENTS

#### *Austria and the Netherlands*

In recent months, the tax authorities in Austria and the Netherlands have started reimbursing dividend withholding tax claims to EU based pension funds. The Dutch tax authorities have said that the decision to reimburse Dutch dividend withholding tax to EU based pension funds was triggered by recent ECJ case law and a recent decision by the Dutch Supreme Court.

The trend set by Austria and the Netherlands is good news for the European pension industry and is very promising for refund requests already filed or that can still be filed by foreign investors in other EU countries.

#### *France*

On 13 February 2009, the French Supreme Administrative Court ruled that the tax treatment of French dividends received by French pension funds under domestic tax law should be extended to EU non-profit organisations of the same nature. Four Dutch pension funds had asked for the annulment of the French Statements of Practice issued in 2005 which deny a withholding tax exemption on French source dividends to non-resident pension funds.

The Court's ruling provides crucial arguments for further litigation in France and may open new opportunities for refund claims in France. The French Government will now need to take a formal position on this. In parallel, the Commission has informed PwC that it welcomes the Court's decision and that it is drafting an EU Reasoned Opinion (second step of the Article 226 EC procedure) against France asking it to comply with EC Law.

#### *Spain*

On 30 April 2009, the Spanish Ministry of the Economy and Finance issued a press release saying it is preparing amendments to the Spanish non-residents income tax act in order to end the discriminatory treatment of non-resident EU (and EEA) based pension funds and that dividends and gains paid to non-resident pension funds will be exempt from taxation.

The Spanish Government's announcement indicates its awareness that the Spanish legislation may well be in breach of EU rules. This is a welcome new development as the Commission announced on 27 November 2008 that it had referred Spain, together with Portugal, to the European Court of Justice under of the Article 226 EC procedure.

### **Czech Republic**

Further to a formal request by the EU in June 2008, the Government has amended its corporate income tax act per 1 January 2009 by extending the exemption from corporate income tax on dividends and interest on bonds and various other securities to EU and EEA based pension funds.

### **Italy**

On 26 June 2008, the Commission issued a Reasoned Opinion against Italy.

### **Estonia and Slovenia**

In November 2008, the Estonian parliament decided to abolish withholding tax on dividends paid to foreign investors from 1 January 2009. Slovenia amended its corporate income tax act in May 2008.

## **SUMMARY**

From the above it transpires that the combined pressure of the PwC-EFRP complaints, the Commission's action against Member States, and favourable ECJ case law and national Supreme Court decisions, is producing concrete results for taxpayers. National governments in the EU have either already aligned their legislation with the EC Treaty or have promised to do so, or they are still negotiating with the Commission such as Denmark, Germany, Finland and Sweden.

## **IMPLICATIONS FOR PORTFOLIO INVESTORS**

Should the ECJ ultimately decide to follow the Commission's reasoning - which is likely given the recent case law - pension funds, which have filed claims in a timely and correct manner, should be granted a refund regarding withholding tax on dividends and interest paid and levied in other EU Member States in breach of the EC Treaty.

To safeguard their rights for previous years and for the future, EU based pension funds should consider filing protective refund requests taking into account local statutory time limits. Non-EU based pension funds e.g. from Australia, Canada, Mexico, Switzerland or the United States, could also consider introducing protective claims since Article 56 of the EC Treaty may also apply to Third Countries.

PwC are advising a great number of pension funds and being the pioneers in this field, we have built up extensive experience in filing refund requests across Europe and facing the local tax authorities on behalf of our clients for the purpose of re-claiming withholding tax on dividends levied in past years. Added to this, we have an excellent relationship with the European Commission.

Our client servicing teams are a mix of dedicated Financial Services professionals and leading EC Tax Law specialists who are able to determine the possibilities based on the actual facts and circumstances that will be an essential element in preparing the cost benefit analysis that should be the starting point for any investor that has suffered withholding tax on EU source dividends.

## **CONTACTS**

If you would like further advice in relation to the issues outlined above, please call your local PwC contact or alternatively any of the people listed below:

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