

Investment Management

Pension Funds can claim back WHT in Europe – Latest developments

In December 2005, PricewaterhouseCoopers' EU Direct Tax Group and the European Federation for Retirement Provision (EFRP) jointly lodged a complaint with the European Commission against 18 EU Member States for their alleged discriminatory taxation of dividend and interest payments to foreign EU pension funds. Based on this initiative, the European Commission started infringement proceedings against nine Member States in May 2007 followed by additional proceedings against five more Member States in the months afterwards. Recent judgments of the European Court of Justice (ECJ) support the Commission's action. Today, four years later, we are beginning to see the fruits of the groundbreaking initiative of PwC and EFRP with the first reimbursements starting in the Netherlands and Austria, and promising developments in France and Spain, and other countries as well.

In 2005, a study by PwC found that most of the EU Member States exempt domestic pension funds from paying corporation and/or income tax and usually also from paying withholding tax on dividend and interest. Even where there is no such exemption at source they normally have access to a refund procedure for claiming back the withholding tax paid.

However, foreign pension funds may not qualify for the relief at source or the refund procedure because the State levying the withholding tax refuses them same treatment as domestic funds. As a result, foreign pension funds end up paying higher taxes on interest or dividends than domestic pension funds.

This differential treatment may dissuade foreign pension funds from investing in other member states and hinders companies in attracting capital from foreign pension funds. According to the Commission, this situation is not justifiable and breaches EC Law, and in particular Article 56 of the EC Treaty on the free movement of capital.

Recent ECJ judgments on direct taxation support this view such as the *Denkavit* case in which the Court has confirmed the principle that outbound dividends cannot 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, a step which involves the repayment of hundreds of millions of Euros. The tax authorities in the Netherlands have said that the decision to reimburse Dutch dividend withholding tax to EU based pension funds was triggered by recent ECJ case law and decisions by the Dutch Supreme Court.

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

France

In 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 refused to exempt Dutch pension funds from withholding tax on French source dividends. The French Supreme Court's ruling provides crucial arguments to pending litigations in France and may open new opportunities for refund claims in France. The Commission has informed PwC that they welcome the position of the French Supreme Court since they are currently drafting a Reasoned Opinion against France on the same issue (second step of the infringement ex Article 226 EC).

Spain

Even though it has not been announced officially, Spanish media have claimed that Spain will amend its domestic legislation before the end of 2009 in order to end the discriminatory treatment of non-resident pension funds. The retrospective effect of this amendment is not clear at this stage but any pension fund which has already submitted "protective claims" in Spain should be affected in a positive way. If the information proves to be true, this would be a very positive new development in Spain especially given that the Commission announced on November 27, 2008 that it referred Spain to the ECJ for not complying with the Commission's formal request to amend its legislation under the Article 226 EC procedure.

Czech Republic

In December 2008, the Czech Government approved changes to the Czech Corporate Income Tax Act regarding the taxation of foreign pension funds from the EU and Norway and Iceland. Foreign pension funds from these countries have become exempt from corporate income tax on dividends and interest on bonds and various other securities. The amendment came into effect on January 1, 2009. In June 2008, the Commission had formally requested the Czech Republic to amend its discriminatory rules against foreign pension funds.

Estonia

In November 2008, the Estonian parliament decided to abolish withholding taxes as of 1 January 2009 on dividends paid to foreign investors, including EU Pension funds.

Slovenia

Slovenia amended its corporate income tax act in line with the EC Treaty in May 2008.

Summary

From the above it shows that since 2005, due to the combined pressure through the PwC-EFRP complaints, the Commission's infringement proceedings, and favourable ECJ judgements and national Supreme Court decisions in the Netherlands and France, is producing concrete results for taxpayers.

EU Member States have either already aligned their legislation with the EC Treaty or they are in the process of doing so or they are still negotiating with the Commission. Italy, Portugal and Spain have not replied satisfactorily to the Commission's request for amending their rules and have received a Reasoned Opinion, and, in the case of Spain and Portugal, have been referred to the ECJ in November 2008.

What does this mean for your investment management portfolio?

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 on other Member states in breach of the EC Treaty.

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

PwC are advising a great number of pension funds. We have extensive experience in filing refund requests in countries around Europe and in facing the local tax authorities on behalf of our clients with the purpose of reclaiming withholding tax on dividends levied in past years. Our client servicing teams are a mix of dedicated Financial Services professionals and leading EC direct tax law specialists, and we look forward to helping you optimise your investment management options.

Contacts

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

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