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Investment Management

UCITS Can Claim Back WHT in Europe – Latest Developments

In 2004, PricewaterhouseCoopers' EU Direct Tax Group (EUDTG) identified the opportunity for, amongst others, investment funds to reclaim EU dividend withholding taxes. As a result of the developments in EU case law by the European Court of Justice, PricewaterhouseCoopers (PwC) has analysed to what extent investment funds that are 'Undertakings for Collective Investments in Transferrable Securities' (UCITS) and organised as corporate funds face tax discrimination when making investments across Europe. PwC found that the imposition of withholding taxes on dividends to such UCITS funds in many EU Member States could constitute an infringement of the free movement of capital as laid down in article 56 of the EC Treaty. In the meantime, we have lodged complaints with the European Commission against 7 EU Member States for their discriminatory taxation of dividend payments to foreign EU investment funds and we have assisted our clients with filing protective claims for investment funds amongst several European jurisdictions for the recovery of EU withholding taxes.

BACKGROUND

Following cases like *Fokus Bank and Denkavit*, the European Court of Justice (ECJ) has raised the issue whether there are possibilities for investment funds to reclaim European withholding taxes. Supported by the recent judgment in the *Aberdeen* case, the ECJ has now confirmed that investment funds investing in equities in EU Member States may wish to consider or proceed filing protective reclaims with the relevant tax authorities to reclaim EU withholding taxes incurred on investment income. Under the laws of several EU Member States, foreign investment funds can not benefit from favourable tax regimes designed for domestic investment funds. As a result, non-resident investment funds end up paying higher taxes on dividends than resident investment funds. This dissuades foreign investment funds from investing in other Member States and domestic companies in attracting capital from foreign investing funds.

According to the European Commission (Commission) and several ECJ cases, this situation is in breach of Community Law, in particular Article 56 of the EC Treaty, the free movement of capital within the EU.

LATEST DEVELOPMENTS

The Aberdeen Case

On 18 June 2009, the ECJ issued its judgment in the Aberdeen Property Fininvest Alpha Oy (Aberdeen) case. In the Aberdeen case the ECJ ruled that an EU Member State levying dividend withholding taxes only on dividends paid to non-resident investment funds, while exempting domestic investment funds from such taxes, is incompatible with the EC Treaty.

This judgment is very welcome news for investment funds that have been subjected to discriminatory taxes on dividends from EU/EEA Member States and marks a significant step forward, confirming the validity of the arguments that PwC has put forward to EU Member State's tax authorities on behalf of its clients and, more importantly, rebutting each of the reasons that tax authorities have presented thus far in rejecting claims.

Belgium

There have been first line discussion with the Belgian tax authorities on the potential restriction/discrimination of EU funds compared to Belgian funds and possible causes of justifications of the different treatment applied. The Belgian tax authorities are currently instructing their files for UK, Irish and Luxembourg funds and asking for more information on the regulatory and tax aspects of the vehicles. The complaint with the Commission against Belgium on behalf of the Investment Management sector is still pending.

Denmark, Spain and Sweden

Complaints have recently been submitted with the European Commission. At this point, no further action has been undertaken by the Commission.

Estonia

There is one claim pending before the Estonian Court of Appeal in which a UCITS is reclaiming Estonian withholding tax. The claim referred to the old regime as withholding tax on dividends in Estonia has been abolished as of 1 January 2009. However, as the statute of limitation is 3 years UCITS managers should still consider their withholding tax exposure in Estonia.

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France

The French government has recently commented on a complaint lodged with the Commission about the difference in taxation of French based UCITS and foreign based UCITS. At the moment, the Commission is preparing a response to the comments by the French government.

In a recent case, the French Supreme Administrative Court held that the preferential tax treatment French pension funds receive should also be granted to EU pension funds that are in a similar situation as French pension funds. Although the case at hand related to pension funds, the case may support the position of UCITS filing claims in France.

Norway

Based on the EEA Agreement and / or domestic rules, legal corporate entities (e.g., banks, insurance companies, UK OEICs) comparable to Norwegian limited companies have been granted refunds of previous paid withholding tax. The Norwegian tax authorities have over the last few years interpreted the domestic tax exemption method narrowly, and several non-resident tax payers have been excluded from its scope of application. However, in September 2009, the Norwegian Ministry of Finance conceded that foreign investors have been taxed in violation of EC Law and will now grant dividend withholding tax refunds.

Poland

In May 2009, the Commission sent a reasoned opinion to Poland. On 6 July 2009, the Polish Government officially acknowledged that its legislation was in breach of EC Law and that appropriate amendments to the CIT Law will be introduced which will come into force per 1 January 2010. EU/EEA foreign pension and investment funds have strong arguments to claim that withholding tax paid in the past on dividends and interest was imposed contrary to EC Law, and they can do so up to 1 May 2004.

SUMMARY

From the above it transpires that several EU governments are moving and are revising their domestic rules to reduce the risk of future reclaims of withholding taxes by UCITS. UCITS managers should keep on monitoring their portfolios to identify opportunities for filing for reclaims of European withholding taxes.

IMPLICATIONS FOR PORTFOLIO INVESTORS

To safeguard their rights for previous and future years, EU based investment funds should consider filing requests and protective claims taking into account local statutory time limitations which differ per Member State, ranging from 3 months to 5 years after payment of the dividend.

Non-EU based investment funds e.g. from Australia, Canada, Mexico, Switzerland or the United States, could also consider filing protective claims since Article 56 EC may also apply to third countries. The Commission believes that third country portfolio investors from outside the EU may in many cases have strong arguments. Although the Commission's focus remains on intra-EU situations, it recently started to pursue the first discrimination complaints filed by third country investors against EU States based on Article 56 EC.

PwC are advising a great number of investment 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. PwC also have an excellent relationship with the Commission.

Our client servicing teams are a mix of dedicated Financial Services professionals and leading EC 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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