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 EU States and domestic companies in attracting capital from foreign pension funds. According to the Commission, this situation breaches EC Law, in particular Article 56 EC, 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, the Netherlands and Norway

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. Austria has amended its pension funds legislation in conformity with EC Law per 18 June 2009

The Norwegian tax authorities have over the last few years interpreted the domestic tax exemption method narrowly, and several non-resident tax payers from the EU 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 start granting dividend withholding tax refunds.

The trend set by Austria, the Netherlands and Norway is good news for the European pension industry and is very promising for refund requests already filed or to 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 ruling provides crucial arguments for more litigation in France and may open new opportunities for refund claims. The Commission has welcomed the ruling and is drafting a reasoned opinion against France.

In September 2009, the French Government sent questionnaires to all non-resident EU pension funds in order to establish the comparability with French "Caisses de retraite et de prévoyance", e.g. to consider them as non-profit bodies according to the French tax doctrine. Claimants should respond within 90 days.

Poland

In May 2009, the Commission sent a reasoned opinion to Poland. In 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.

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 to end the discriminatory treatment of non-resident EU based pension funds, and that per 1 January 2010, dividends and gains paid to non-resident pension funds will be exempt from taxation. This is a welcome new development after the Commission's referral of Spain (and Portugal) to the ECJ, as announced on 27 November 2008.

Italy and the Czech Republic

Further to a reasoned opinion received from the Commission on 26 June 2008, the Czech CIT Act has been amended since January 2009 extending the exemption from corporate income tax on dividends and interest, bonds and other securities to EU pension funds. Italy also received a reasoned opinion on 26 June 2008 but no further actions have been undertaken yet.

Denmark and Finland

On 25 June 2009, the Commission sent Denmark and Finland reasoned opinions to change their legislation to end the discriminatory taxation against foreign pension funds (second step of the EU infringement proceedings under Art. 226 EC).

Estonia and Slovenia

Estonia abolished withholding tax on dividends paid to foreign investors on 1 January 2009. Slovenia amended its CIT Act in May 2008.

SUMMARY

From the above it transpires that the combined pressure of the PwC-EFRP complaints, the Commission's action against EU Member States, and favourable ECJ case law and national Supreme Court decisions, is producing concrete results. EU governments 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 Germany.

IMPLICATIONS FOR PORTFOLIO INVESTORS

Should the ECJ decide to follow the Commission's reasoning, which is increasingly likely given the recent case law and developments, pension funds, which 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 EC Law.

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 U.S., could also consider introducing protective claims since Article 56 EC may also apply to third countries. Third country portfolio investors from outside the EU have strong arguments. Although the focus of the Commission remains on intra-EU situations, it recently started to pursue the first discrimination complaints filed by third country investors against EU Member States based on Article 56 EC.

PwC are advising a great number of pension funds and being the pioneers in this field, we have built up extensive experience in filing protective refund requests across Europe and facing the local tax authorities on behalf of our clients. Added to this, we have an excellent relationship with the 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:

Martin Vink	+ 31 20 568 6445	martin.vink@nl.pwc.com
Bob van der Made	+ 31 10 407 6781	bob.van.der.made@nl.pwc.com