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EU Direct Tax Group

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The EUDTG is one of PwC's Thought Leadership Initiatives and embedded in the International Tax Services Network. The EUDTG is a pan-European network of EU tax law experts and provides assistance to organizations, companies and private persons to help them to fully benefit from their rights under EU law.

The ECJ gave its decision in the Denkavit French dividend withholding tax case (C-170/05) in favour of the foreign parent company

Denkavit International BV (DI BV) held 99.9% of share capital of a French subsidiary Agro-Finances Sarl (AF Sarl), which in turn held 50% of another French company Denkavit France Sarl (DF Sarl), the other 50% of DF Sarl being held directly by DI BV.

In the years 1987 to 1989 (before the Parent/Subsidiary Directive was in force), AF Sarl and DF Sarl paid dividends of 14.5 million French Francs to DI BV, from which 5% French withholding tax was deducted, in accordance with French domestic tax law and the Dutch/French double tax treaty.

The French Conseil d'Etat referred the case to the ECJ, asking whether the imposition of dividend withholding tax by France on dividends only to non-resident parent companies (including fellow members of the EU) as compared with, in almost all circumstances, the absence of French dividend withholding tax on dividends paid by similar French subsidiaries to a French parent company, as defined by French tax legislation, was contrary to Article 43 (freedom of establishment) of the EC Treaty.

In addition, the Conseil d'Etat also asked whether the provisions of the Dutch/French tax treaty whereby a Dutch parent company was obliged to give a credit for the French dividend withholding tax up to the corresponding level of any Dutch tax - even if, in practice, no such ordinary credit was given by the Netherlands because of the Dutch participation exemption - altered the analysis.

The ECJ stated that such difference in the tax treatment of dividends between parent companies, based on the location of their registered office, constitutes a restriction on freedom of establishment, which is prohibited by Articles 43 and 48 of the EC Treaty and incapable of justification.

In addition, the Court considered that the provisions of the Dutch/French tax treaty are to be taken into account in assessing the compatibility of the French withholding tax with Article 43 EC. The ECJ however held that the combined application of the Dutch/French tax treaty and the Dutch participation exemption regime does not serve to overcome the effects of the restriction when the Dutch parent company is unable to offset the tax credit provided by the double tax treaty.

Whilst the opinion deals only with freedom of establishment, it is considered highly likely that the outcome will be the same in a portfolio situation i.e. one covered by free movement of capital. It is therefore another indication that treating resident and non-resident shareholders differently for dividend withholding tax purposes is not in line with the free movement of capital. The conclusion supports for example the complaints PwC has submitted (together with the European Federation for Retirement Provision) claiming that dividend distributions to foreign pension funds should not be subject to a less favourable withholding tax treatment than dividend distributions to domestic pension funds.

Claims for refund can be filed in France up to 31 December 2008, in respect of withholding taxes paid as from 2003.

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