

Newsalert

EU Direct Tax Group

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ECJ judgment in the *Meilicke* case, C-292/04 - tax credit on foreign dividends

Mr. Meilicke, a German resident individual, received dividends from Dutch and Danish companies in 1995 through 1997. In 2000, the heirs of Mr Meilicke applied unsuccessfully for an imputation (tax) credit on those dividends, which would have been granted on dividends paid by German resident companies under the former German imputation system. The Tax Court of Cologne referred the case to the ECJ and asked if the rules were in breach of the free movement of capital. The imputation system was abolished in 2000.

The ECJ pronounced its judgment on March 6, 2007. The outcome was as expected in respect of the material issue, namely if Germany had to grant an imputation credit on foreign dividends where a credit was granted on dividends paid by resident companies: The rules of the former German imputation system constitute a breach of the free movement of capital, just as the ECJ had decided that the more or less identical Finnish imputation system was in breach of the free movement of capital in the *Manninen* judgment, C-319/02, as of September 7, 2004. The German imputation credit was calculated by reference to the underlying corporation tax on the distributed dividend. The same should, according to the argumentation in the ECJ judgment, apply for the credit on foreign dividends, even if the foreign underlying corporation tax is higher than the German one.

Due to the German government's application for a temporal limitation of the effects of the judgment, there were two Advocate Generals' opinions in the case (see [NA 2005 - 013](#) and [NA 2006 - 030](#)) and it was decided by the Grand Chamber.

- Germany argued that an unlimited application would lead to grave financial consequences and further that Germany was in good faith concerning a possible breach of Community law at least until the *Verkoojen* judgment (C-35/98) by the ECJ on June 6, 2000.
- In 2005, AG Tizzano opined that a limitation of the temporal effects was justified.
- In 2006, AG Stix-Hackl opined that Germany's application for a temporal restriction in the *Meilicke* case was not precluded by the fact that the ECJ had already interpreted the relevant Community law provision (here, the free movement of capital) in earlier judgments, e.g. *Verkoojen* (2000) and *Manninen* (2004), without limiting the temporal effects of those judgments. However, the AG was of the opinion that Germany had failed to prove grave economic consequences required to limit the temporal effects and also questioned whether Germany had been in good faith concerning the uncertainty of the application of EU-law prior to the *Verkoojen* judgment.

The ECJ now clarified the issue of a limitation of temporal effects. There must be *one* single occasion when a decision is made on the temporal effects of the interpretation on Community law. The principle that a temporal restriction is only allowed in the *actual judgment ruling on this interpretation* ensures legal certainty and that all Member States and other subjects of Community law are treated equally. The *Meilicke* case concerns the tax treatment that a Member State has to accord to foreign dividends. The *Verkoojen* case of 2000 already dealt with the requirements arising from the free movement of capital in respect of foreign dividends received by residents. Since the temporal effects of that judgment were not limited and, additionally, the principles were confirmed in e.g. the *Manninen* judgment, the ECJ did not find it appropriate to limit the temporal effects of the *Meilicke* judgment. There was therefore no need to go into details on the German government's argumentation in respect of grave economic consequences and good faith.

The judgment by the ECJ certainly makes it more difficult for Member States to successfully apply for a limitation of the temporal effects in future cases. Apart from proving the grave economic consequences of an unlimited application and their good faith in respect of uncertainty of Community Law interpretation, the Member States now also have to convince the ECJ that the cases previously decided did not concern the same or a similar issue.

It remains to be seen what kind of proof the German tax authorities will require from the tax payers in respect of the underlying corporation tax paid on foreign dividends. Seeing that the German government calculated with tax repayments of ca Euro 5 bn if the temporal effects of the judgment were not limited, the burden of proof on the tax payer must - at least for the purposes of that calculation - have been set at a rather moderate level.

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