CJEU rules that Portugal's withholding tax on dividends paid to non-resident investment funds is incompatible with EU Law

On 17 March 2022, the Court of Justice of the European Union (CJEU) rendered its judgment in the AllianzGI-Fonds AEVN case (C-545/19) finding that Portuguese withholding tax on dividends paid to non-resident investment funds is in breach of EU Law.

The fact of the case

The case originated from an appeal lodged before the Portoguese Tax Arbitration Court (CAAD) by AllianzGI-Fonds AEVN, an open-end collective investment undertaking (UCITS) established under German law in accordance with Directive 2009/65/EC which requested the full reimbursment of the dividend withholding tax suffered in Portugal with respect to Portoguese-sourced dividends received during the years 2015 and 2016 because levied in breach of EU law.

The CAAD referred the case to the CJEU asking whether the Portoguese legisation by providing for the levy of withholding tax on dividends distributed to non-resident UCITS while exempting Portoguese UCITS from taxation on the same type of Portoguese-sourced income, led to a breach of either article 56 TFEU on the freedom to provide services or article 63 TFEU on the free movement of capital.

On the basis of the applicable domestic legislation, in fact, dividends paid by Portuguese resident companies to Portuguese tax resident UCITS are exempt from corporate income tax. Taxation occurs solely at investor's level in case of an income distribution or redemption of participation units. Resident UCITS are in any case subject to stamp duty tax on their net asset value at a 0.0025% or 0.0125% rate (depending on the type of investment). Differently, dividends paid by Portuguese resident companies to non-resident UCITS are subject to a 25% withholding tax (or the reduced double tax treaty rate if applicable).

The CJEU's judgment

The CJEU concluded that Article 63 TFEU must be interpreted as precluding Portoguese legislation from levying dividend withholding taxes towards non-resident UCITS while dividends distributed to a resident UCITS are exempt from such withholding tax. In particular the CJEU ruled that:

i) the Portuguese legislation is as such as to discourage, on one hand, non-resident CIUs from investing in companies established in Portugal and, on the other hand, investors resident in Portugal from acquiring shares in UCITS, being, as such, a restriction on the free movement of capital precluded in principle by Article 63 TFEU;

ii) the difference in treatment between resident and non-resident UCITS concerns objectively comparable situations, notwhistanding stamp duty tax being levied on the net asset value of resident UCITS;

iii) this difference in treatment may not be justified by overriding reasons in the public interest, namely the need to preserve the coherence of the tax system, and the balanced allocation of taxing rights.

Takeaway

This judgment is of great impact to non-resident UCITS and other similar non-resident investment vehicles. Those entities may in fact claim withholding tax incurred in Portugal in the last four years, as well as any withholding tax being applied until the Portuguese legislation is amended to reflect the conclusions of the CJEU's Judgement.

Let's talk

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