EUDTG Newsalert
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CJEU sets position concerning discrimination towards loss making Entities with tax residence outside Spain: Biscay law infringes the free movement of capital

According to the Court of Justice of the EU (CJEU) in case C-601/23 (C 601/23), the non-residents income tax Act of the territory of Biscay infringes Article 63 TFEU due to the fact that the said regulation does not allow non-resident entities that end a fiscal year with a loss, to claim a refund of withholding taxes levied on dividends paid by companies resident in the territory of Biscay, while conversely the corporate tax Act of the territory of Biscay recognizes the right to obtain a refund of withholding taxes suffered by resident entities in the same loss making situation.

Background and facts

The CJEU ruled on a case concerning the taxation of dividends paid by a Spanish company to a UK company, finding a discriminatory practice against non-resident companies that, unlike resident companies, did not receive refunds of withholding taxes levied when they recognised a loss for a fiscal year.

The case involved Credit Suisse Securities (Europe) Ltd, a UK company with no permanent establishment in Spain that had received dividends from a company domiciled in Biscay, a territory with fiscal autonomy within Spain. The dividends were subject to a 19% withholding tax on the gross amount, which was reduced to 10% under the Spain-UK double tax treaty. However, Credit Suisse Securities (Europe) Ltd could not claim a credit for the Biscayan withholding tax in the UK, as it had losses in the year of receipt of the dividends and no taxable income.

Credit Suisse Securities (Europe) Ltd applied for a refund of the withholding tax in Biscay, arguing that it was subject to a different and less favourable treatment than a resident taxpayer. Had Credit Suisse Securities (Europe) Ltd been a resident of Biscay, it would be subject to corporate income tax only on its remuneration for its services, with a net corporate income tax base of zero for the dividends, as costs from increased obligations to clients would be deductible. Moreover, the withholding tax would be fully offset against the corporate tax payable or refunded in case of losses.

The Biscayan tax authorities rejected the refund claim, as well as the subsequent administrative appeal. Credit Suisse Securities (Europe) Ltd then brought a judicial action before the High Court of Justice of the Basque Country, which referred the case to the CJEU for a preliminary ruling on the interpretation of Article 63 TFEU on the free movement of capital.

CJEU's judgment

The CJEU found that the Spanish tax law, which does not allow refunds for non-resident companies in cases of losses, constitutes a restriction on the free movement of capital, contrary to EU law. The CJEU, following a request for a preliminary ruling from the High Court of Justice of the Basque Country, held that the Biscayan tax law was incompatible with Article 63 TFEU.

- **Different tax treatment:** The CJEU noted that the withholding tax applied to non-resident companies was different from the one applied to resident companies, which was equivalent to an advance payment of the corporate income tax and was fully refunded in case of losses. The CJEU considered that this difference of treatment amounted to a disadvantage for non-resident companies, which could deter them from investing in the Basque country (and, more broadly, Spain) or vice versa, and thus constituted a restriction on the free movement of capital.

- **Tax collection assurance does not justify the discrimination:** The CJEU also rejected the justifications put forward by the Spanish tax authority and the governments of Spain and Germany, which invoked the need to ensure the effective collection of taxes, the preservation of the balanced allocation of taxing powers between the Member States, and the prevention of the double use of losses. The CJEU found that none of these objectives could justify the immediate and definitive taxation of dividends paid to non-resident companies in case of losses, where resident companies in the same position benefited from a refund or a deferral of taxation.

- **The competent tax authorities are obliged to use the mutual assistance mechanisms:** The CJEU pointed out that non-resident companies could provide the relevant evidence to prove their losses and that the existing mechanisms of mutual assistance between the tax authorities of the Member States were sufficient to allow the verification of such evidence.

- **Double Tax Treaty reduced rates do not neutralize discrimination:** The CJEU also stressed that the lower tax rate applied to non-resident companies through the application of the applicable double tax treaty did not compensate for the disadvantage resulting from the withholding tax.

The judgment confirms the principle that Member States cannot discriminate or restrict the free movement of capital based on the residence of the companies that receive dividends from domestic sources, unless they can prove that such measures are necessary and proportionate to achieve a legitimate objective.

Takeaway

In Credit Suisse Securities (Europe), the CJEU confirmed its previous case law on the equal tax treatment of dividends paid to resident and non-resident companies, especially the Sofina and others (C-575/17) and ACC Silicones (C-572/20) judgments. According to the CJEU, there is no justification for differentiating non-resident loss making entities against resident entities in the same situation, when the latter have the right to obtain a refund for withholding taxes suffered while the former do not.

For non-resident entities in Spain with pending dividend withholding tax claims, this judgment can be considered a positive development. However, the judgment may also have implications for other investors in similar economic positions (i.e. loss-making entities), or for other sources of income subject to withholding tax (e.g. interests, royalties).

The judgment may also have implications relevant for both the Spanish central tax regulations and other Member States that apply similar withholding taxes on dividends paid to non-resident companies.

Let's talk

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