EU Direct Tax Newsalert

CJEU judgment on Danish withholding tax on dividend payments to non-resident investment funds

On 21 June 2018, the Court of Justice of the European Union (CJEU) issued its judgment in *Fidelity Funds* (C-480/16). The underlying question of the case was whether it is in accordance with the free movement of capital that non-resident investment funds are subject to withholding tax on dividends received from their Danish portfolio investments while resident investment funds are exempted from withholding tax on such dividend payments.

Case facts

Fidelity Funds, Fidelity Investment Funds, and Fidelity Institutional Funds ("Fidelity") are resident in the United Kingdom and Luxembourg and qualify as Undertakings for the Collective Investment of Transferable Securities (UCITS) covered by Directive 85/611/EEC. Fidelity invested in Danish portfolio shares. In the years 2000-2009, it received dividends from Danish portfolio shares which were subject to withholding tax. Contrary to Fidelity, resident investment funds were exempt from withholding tax on dividends from Danish portfolio shares, and Fidelity therefore filed a claim for repayment of withholding tax levied on the dividend distributions. It is a condition in order for resident investment funds to benefit from the tax exemption that they must elect a status as distributing fund in accordance with the rules set out in section 16 C of the Danish Tax Assessment Act (DTAA).

The CJEU judgment

Fidelity and the Danish Ministry of Taxation agreed that there is a difference in treatment between resident and non-resident investment funds, and that the difference in treatment constitutes a restriction on the free movement of capital. The Danish Ministry of Taxation, however, claimed that the restriction was justified, first, by the need to safeguard the coherence of the tax system and, second, by the need to ensure a balanced allocation between the Member States of the power to impose taxes.

The CJEU first held that the situations of the resident and non-resident investment funds were objectively comparable in the light of the objective of the law which was to avoid economic double taxation by only taxing the members of the investment fund. If both the investment funds and their members were taxed, economic double taxation would occur.

The CJEU then considered that the taxation of non-resident investment funds on dividend payments from Danish companies cannot be justified by the need to ensure the allocation of taxing powers as Denmark had chosen not to tax resident investment funds on similar dividend payments.

The CJEU held that the need to safeguard the coherence of the Danish tax system could in principle, constitute a justification for the restriction, however that the restriction went beyond what was necessary in order to safeguard the coherence of the Danish tax system. Thus, the CJEU stated that it could be a less restrictive measure, if the non-resident investment funds were allowed to calculate income according to the minimum distribution calculations set out in section 16 C of the DTAA.

The CJEU therefore concluded that the restriction could not be justified by the need to safeguard the coherence of the Danish tax system, and that the Danish rules were in breach of EU law.

Takeaway

Based on the CJEU's judgment, non-resident investment funds – both UCITS and non-UCITS – should be entitled to reclaim taxes withheld on dividend payments from Danish portfolio shares.

As the CJEU judgment concerns the free movement of capital, investment funds resident in third countries should also, in principle, be able to file a claim.

The case is scheduled for a hearing before the Danish High Court in February 2019.

In the meantime, we recommend that foreign investment funds file protective claims in order to avoid potential claims from being statute barred. Claims should be filed for years back to 2008.

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