

## // Italian dividend WHT: is the door opening?

The European Court of Justice ("ECJ") found that the Italian dividend withholding tax ("WHT") system (before being amended in 2009) was in breach of article 56 (1) of the EC Treaty, which prohibits all restrictions on the movement of capital between member states and between member states and third countries. Prior to 2009, Italy exempted 95% of the dividends paid to Italian companies and taxed at 33% the remaining 5% whereas it charged at 27% dividend distributions to EU and EEA companies, taxing them at a higher rate, which is why the European Commission decided to refer Italy to the ECJ.



PHOTO Keith O'Donnell

The court rejected the argument of Italy that the tax levied there on distributions to non-Italian companies would be creditable in the country of the foreign parent company based on a double tax treaty ("DTT") as the possibility to effectively credit the tax depended on the specific situation (the foreign tax may not necessarily be high enough to credit the Italian tax in full and Italy does not have tax treaties with all EU and EEA countries).

### // Non-member states different

The ECJ also dismissed the argument made by Italy that an Italian individual would be taxed on the dividend received in a similar way as the foreign shareholder, as it amounted to comparing two incomparable situations. The ECJ referred to previous jurispru-

dence to conclude that a breach of article 56 could not be justified to fight against tax evasion in the case at hand, as a general presumption of tax avoidance or evasion could not justify a tax measure which adversely affected the objectives of the EC Treaty.

The ECJ indicated that the case law concerning restrictions on the exercise of freedom of movement within the Community could not be transposed in its entirety to movements of capital between member states and non-member countries, since such movements take place in a different legal context. In the case at hand, the ECJ considered the breach of the EEA Treaty as justified in absence of an exchange of information system between Italy and the country of the investor.

Outstanding questions remain however: what level of exchange of information is considered as sufficient to fight against tax evasion? Is it possible to conclude, interpreting *a contrario*, that if an exchange of information system is in place, no restriction to the exercise of freedom of movement between member states and non-member countries is allowed to fight against tax evasion? It is regrettable that the Commission did not pursue this point further in its action.

### // Luxembourg legislation impacted?


Given its Luxembourg WHT exemption regime, which applies under certain threshold conditions, to dividends distributed to EU

and EEA undertakings as well as to companies that are resident in a DTT country, the Luxembourg legislation should *prima facie* be considered as in line with the ECJ jurisprudence commented.

Luxembourg tax legislation may however not be fully compliant with the C-194/06 jurisprudence in situations where the tax levied in the source country (Luxembourg) is higher than the tax due in the country of the parent company: in such situations, while Luxembourg investors are entitled to a reimbursement of the difference between the amount of WHT and the amount of tax finally due in Luxembourg, a foreign investor is not and this treatment may be considered as discriminatory.

### // What does this decision mean for non-EU companies/funds investing in Europe?

Despite the fact that the position taken by the ECJ as regards non-EU countries is based on article 40 of the EEA Agreement, this decision and the decision in Case C-101/05 (this one based on article 56) seem to increase the chances for non-EU funds to recover WHT suffered in their EU investment countries and they should consider introducing claims or at least protective claims to get a reimbursement of WHT, even if this claim may probably end up in front of the ECJ. We have been assisting clients in cases in this regard, the amounts involved can be significant so the budgetary impact is a factor, especially in the current fiscal environment.

 By Keith O'Donnell, Managing Partner and Samantha Nonnenkamp, director. The authors work for ATOZ, a member of the Taxand network.