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Art. 63 Refunds of WHT – European Court decision helps German refunds (ACC Silicones case)

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An important decision was given yesterday striking down a German provision that required foreign investors to demonstrate "no offset" of German withholding taxes ("**WHT**") in order to get a refund. This will facilitate thousands of claims by EU and non-EU investors.

The decision is of high importance as currently more than 30,000 WHT reclaim applications are pending with the Federal Tax Office which, hopefully, could move closer to a resolution following this decision.

The decision follows an opinion of Advocate General Collins ("**AG**") issued a few months ago in the case.

Background

The request for preliminary ruling was filled by the Finance Court in Cologne, Germany. The claimant in the main dispute, ACC Silicones Ltd ("**ACC**"), a company established in the UK, held a minority shareholding in a German resident company, Ambratec GmbH ("**Ambratec**") between 2006 and 2008. Upon distribution of dividends by Ambratec to ACC, 25.5% WHT was levied.

In two separate applications, ACC requested refunds of a) the WHT up to 15% based on the provisions of Paragraph 50d (1) of the *Einkommensteuergesetz* ("**EStG**") and of Article VI(1) of the convention for the avoidance of double taxation concluded between Germany and the UK ("**DTT**"), and b) the balance of the WHT suffered based on Art. 63 of the Treaty on the Functioning of the European Union ("**TFEU**").

The first part of the claim was granted and the WHT up to 15% was reimbursed. The second part of the applications was rejected by the German tax authorities, with the argument that the conditions laid down in Paragraph 32 (5) of *Körperschaftsteuergesetz* ("**KStG**") has not been fulfilled. In fact, according to the Finance Court in Cologne, hearing ACC's appeal, all the conditions were met except the condition laid down in the second

sentence of Paragraph 32(5) of the KStG. Following that condition, the reimbursement is granted only if the disadvantage to foreign recipients as compared to domestic dividend recipients cannot be equalised by set-off, deduction from the basis for tax assessment or carry forward of the set-off in the country of residence of the recipient of the dividends (in this case the UK). ACC was also required to prove that the conditions were met by submitting a certificate from the UK tax authorities, stating that the German WHT cannot be offset, deducted, or carried forward and that no such offsets have actually taken place. This information needed to be provided for both ACC and all direct and indirect shareholders in the company.

During the proceedings, ACC failed to provide this information for its shareholders.

In this situation, the Finance Court of Cologne queried firstly if the rules set out for reimbursement of WHT suffered by non-resident companies were contrary to Art. 63 of the TFEU. More specifically, the rules applicable to local resident companies differed from those applicable to non-resident companies, i.e. local companies did not need to provide a proof that the WHT suffered was not offset, deducted or carried forward by their investors.

Secondly, in case that these rules were considered compatible with Art. 63 TFEU, the FCC asked whether those rules comply with the principles of proportionality and effectiveness as it is practically impossible for foreign companies to provide such proof.

The referral to the Court of Justice of the European Union ("CJEU") was submitted on 3 November 2020.

AG opinion

According to the AG Collins opinion, the questions raised revolve not so much around the evidential requirements set out in the German legislation as the principle of the requirements. In his view, if as a matter of principle, the additional conditions for foreign investors set out in Paragraph 32(5) of the KStG are to be seen contrary to Art. 63 TFEU, this should automatically apply to the actual evidential requirement.

While drawing his conclusions, he also analyses if the restrictions resulting from the German legislation could be justified under Art. 65 (1)(a) TFEU[1] as well as various CJEU jurisprudence.

The AG saw the German legislation discriminatory towards non-resident companies, as the right of reimbursement of WHT was subject to stricter conditions than for resident companies and considered such treatment as discouraging non-resident companies from investing in German companies. Furthermore, no justification of such treatment was obvious to the AG as the situations of resident and non-resident companies were comparable and no overriding reason in the public interest existed.

As a conclusion, the answer suggested by the AG to the first question was that Art. 63 TFEU precludes national provisions such as the one in question and the source State must reimburse the WHT not offset under the provisions of any applicable DTTs.

With regards to the second question, for sake of completeness, the AG firstly recalled that, while Member States can determine what sufficient evidence is required in order to benefit from a tax advantage, such fiscal autonomy must be carried out in accordance with the requirements of the EU law and in particular the provisions related to the free movement of capital. The AG then concluded that in this case, evidential requirement imposed by the German legislation was disproportionate and posed considerable difficulties for ACC.

[1] "The provisions of Article 63 shall be without prejudice to the right of Member States: (a) to apply the relevant provisions of their tax law which distinguish between taxpayers who are not in the same situation with regard to their place of residence or with regard to the place where their capital is invested".

Decision of the CJEU

With regards to the first question, the Court first concludes that the situation of resident and non-resident companies is comparable as Germany applies similar WHT treatment to dividend distributions to both resident and non-resident companies.

The difference in treatment that is obvious in the case at hand can only be eliminated if the country of residence of ACC (UK) offsets fully the WHT suffered in Germany. This offset is uncertain and more burdensome than the direct credit offered to resident companies in comparable situation. Therefore, this possible offset cannot be relied upon to eliminate the difference in treatment.

The Court, like the AG, was not able to find a reliable justification for the discriminatory treatment towards non-resident companies. On the contrary, the Court concludes that the system applied by the German legislation is unreliable for the purposes of avoiding double taxation and double offset of the WHT suffered by non-resident companies.

As a conclusion, the Court found that the provisions laid down in the second sentence of Paragraph 32(5) of the KStG are contrary to Art. 63 TFEU.

Following the answer given to the first question, the Court decided that answering the second question is not relevant.

Conclusion

The case decided by the CJEU is important for pending WHT reclaims, as the “no set-off” evidence requirements in the German legislation constitute an infringement of the free movement of capital, as such evidence is not required from a company domiciled in Germany. While not the core of the decision, the AG opinion on evidential requirements being disproportionate is also encouraging.

Although the decision is positive for the taxpayer, it should be noted that wide application to all pending cases might not be possible. After 28 February 2013, a new version of section 8b (4) of KStG was introduced. Accordingly, all dividend payments became taxable, thus potentially eliminating the disadvantageous treatment of cross-border dividend payments.

A decision from the referring Court following this should shed even more light on the situation and hopefully allow the German tax authorities to take a position on at least some of the pending case.

Do you have further questions?

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