Belgian Tax Authorities Explain Consequences of ECJ Judgment

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Belgian tax authorities on March 4 published Practice Note Ci.RH.233/623.711 on the tax consequences of the European Court of Justice's October 25, 2012, judgment in *Commission v. Belgium* (C-387/11).

The Case

The case regarded Belgian rules that impose a withholding tax on dividends and interest paid to resident and nonresident investment companies.

For Belgian-resident investment companies, such income is exempt from company income tax (article 185 *bis* Income Tax Code 1992), so it can be credited and refunded. Nonresident investment companies, however, incur a definitive withholding tax liability and cannot offset or claim a refund of the withholding tax unless they have a permanent establishment in Belgium.

The ECJ ruled that the Belgian rules infringed both the free movement of capital and the freedom of establishment under both the Treaty for the Functioning of the European Union (TFEU) and the European Economic Area Agreement of May 2, 1992.

The Court referred to its previous case law when examining the objective comparability of resident and nonresident funds. Taxing both resident and nonresident funds on income derived from a Belgian-resident company means that the funds are in comparable situations. When this results in double taxation, the ECJ says, it is up to the payer's EU member state of residence to ensure that resident and nonresident companies are treated the same way (see, for example, the judgments in *FII Group Litigation* (C-35/11) and *Amurta* (C-379/05)).

In *Commission v. Belgium*, Belgium argued that the taxation of unit holders should be taken into consideration. However, the ECJ referred to its decision in *Santander* (joined cases C-338/11 to C-347/11), stating that the sole distinguishing criterion in the legislation at issue is the country of residence of the investment company; therefore, the comparison should be made at the company level.

Belgium also argued that the different treatment was justified on the grounds of the balanced allocation of taxing powers. The Court rejected that argument; in extending the rules applicable to resident companies to nonresident companies that do not have a Belgian PE, Belgium is not giving up its right to tax that income because it has already taxed the income in the hands of the Belgian-resident company distributing its profits, the Court said.

Another ground for justification brought by Belgium was the need for effective fiscal supervision. The ECJ also rejected that argument, stating that nonresident companies are not, under any circumstances, able to enjoy the benefits provided to resident companies in this context (that is, even if they were in a position to provide the necessary assurance).

Belgium's final argument that income tax treaties neutralize the different treatment also failed to impress the Court, which noted that previous similar cases have shown that treaty provisions do not have that effect in all cases.

The Court also denied Belgium's request for a temporal limitation on the effects of the decision, saying that Belgium's approximate quantification of the amount of withholding tax that would potentially need to be refunded did not sufficiently demonstrate a risk of serious economic repercussions.

Consequently, the ECJ held that by maintaining different rules for the taxation of income from capital and movable property based on whether it is earned by resident or nonresident investment companies without a PE in Belgium, the country failed to fulfill its obligations under articles 49 and 63 of the TFEU and articles 31 and 40 of the EEA Agreement.

The Practice Note

In the March 4 practice note, the tax authorities confirmed that foreign Undertakings for Collective Investment in Transferable Securities (UCITS) established in an EU member state or the EEA are entitled to a refund of the tax withheld on dividends paid between May 1, 2007, and December 31, 2012. The note announced that new legislation will be passed to comply with the decision and will have retroactive effect from January 1.

UCITS established outside the EEA are also entitled to the refund if they are comparable to EU UCITS (that is, if they meet all the criteria of Directive 85/611/EEC) and if they are established in a country with which Belgium has signed an income tax treaty that provides for exchange of information between the tax administrations or allows the application of domestic legislation on exchange of information.

These foreign UCITS will be entitled to a full or partial refund if they provide evidence that they cannot (fully or partially) credit the Belgian withholding tax against their tax liability in their state of residence because they are exempt from tax, sustain losses, or pay an insufficient amount of corporate income tax, or if they can prove that foreign withholding tax is not refunded in their state of residence. The refund will be limited to the part of the withholding tax that is not credited or refunded in the state of residence.

UCITs that are entitled to a refund but have not yet filed an appeal will have six months from the date of publication of the practice note to do so. A withholding tax refund cannot be claimed after five years from January 1 of the year in which the withholding tax was withheld, or if no notification regarding the withholding tax was received.

Comments

Although the ECJ denied Belgium's request for a temporal limitation on the effects of the judgment, the practice note refers only to dividend withholding tax levied after January 1, 2007. However, taxpayers that filed protective refund claims before 2012 will be eligible for refunds of taxes levied before that date, based on the application of the five-year statute of limitations.

The practice note does not address the parallel issue of the discriminatory tax treatment of interest paid to foreign investment funds. The ECJ did, however, mention the taxation of income from capital and movables, which includes interest.

The practice note also announces further guidelines for refunds to companies that do not qualify as UCTIS, following the ECJ's judgment in *Tate & Lyle Investments* (C-384/11). (Prior coverage.)

Marc Quaghebeur, partner, De Broeck Van Laere & Partners, Brussels