European Court of Justice rules: refusal to refund withholding tax on dividends to European parent companies violates European Law

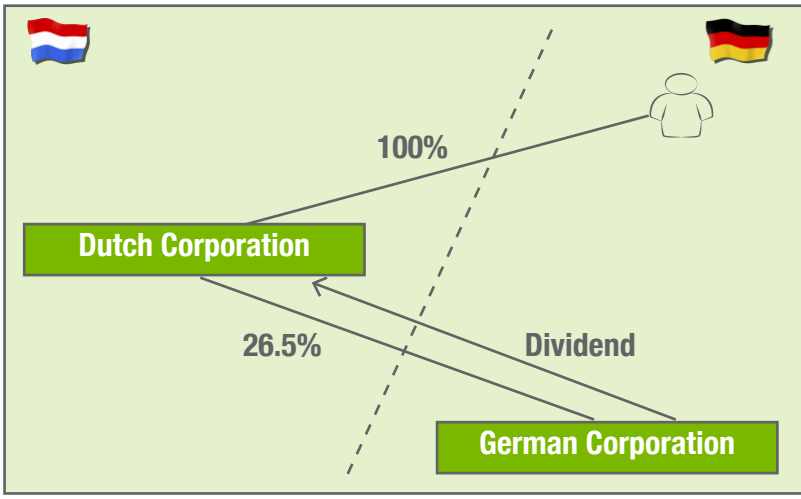
February 14, 2018

Shortly after the French anti-abuse rule for the Parent-Subsidiary-Directive was declared void because it was contrary to European law, the German rule is next. In the joined cases C-504/16 (Deister Holding) and C-613/16 (Juhler Holding), the European Court of Justice decided that the anti-abuse rule of Section 50d (3) German Income Tax Act in the version of 2007 violates both the Parent-Subsidiary-Directive and the freedom of establishment. Even though the judgement is only applicable for cases until the assessment year 2011, there are substantial doubts that the new version which is valid since 2012 is in line with European law. This question is indeed already on the table of the European Court of Justice (ECJ C-440/17).

In both the Deister Holding and the Juhler case, the German fiscal authorities denied a refund of withholding tax on dividends to European parent companies. The Deister Holding was resident in the Netherlands and had a share of 26.5 percent in a German corporation (GmbH). The Deister Holding itself was owned by a German individual. The German corporation distributed a dividend to the Deister Holding and withheld tax and solidarity surcharge. Normally, under Section 50d (1) German Income Tax Act (in connection with Section 43b German Income Tax Act the German implementation of the Parent-Subsidiary-Directive), the German fiscal authorities would refund the withheld tax to the foreign corporation (here the Deister Holding). However, the German authorities denied this refund because they argued that the Deister Holding would not have an own economic activity, as it was a mere holding corporation without any business activity. The Juhler case was basically similar. Juhler was a holding corporation in Denmark with a share in a German corporation. Juhler itself was owned via a holding company in Cyprus by an individual in Singapore. The refund of the withholding tax on the dividend of the German corporation was also denied for Juhler.

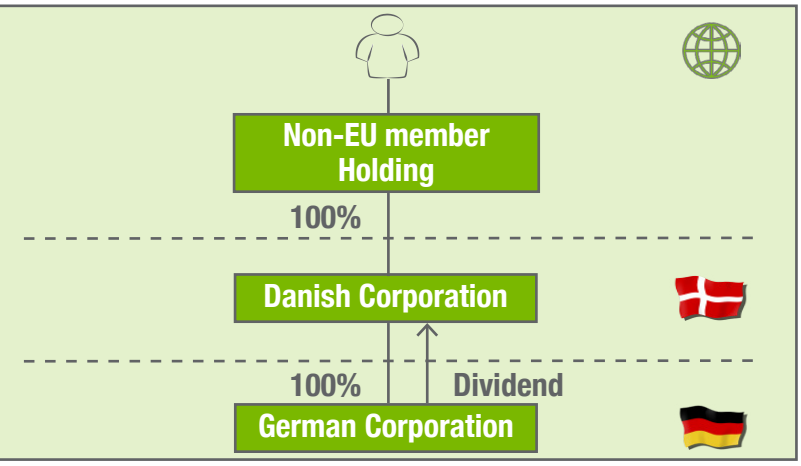
Documents to beinformed:

- C-504/16 and C-613/16



The European Court of Justice already decided for the French anti-abuse rule regarding the Parent-Subsidiary-Directive (“Eqiom and Enka” judgement of September 7th, 2017, C-6/16) that a general abuse assumption, as it was laid out in the French tax act, is not in line with European Law. The rules to determine that an arrangement is wholly artificial should not be on a simple general basis resulting in even non-abusive arrangement falling under the scope of the rule. In contrast, the arrangements have to be assessed on a case-by-case basis based on factors including the organizational, economic or substantial features of the group of companies to which the parent corporation in

question belongs. The German anti-abuse rule for the Parent-Subsidiary-Directive in the version of 2007 was by and large similar to the French rule. It contained only general clauses concerning economic reasoning, own economic activities or general economic commerce with other businesses. By that, it constitutes a general abuse assumption, which violates European law (i.e. it violates both the Parent-Subsidiary-Directive and the freedom of establishment).



As outlined above, the European Court of Justice decided for European cases on the old German anti-abuse rule which was valid for fiscal years until 2011. However, there are two further aspects of the judgement one should take away: First, even the new rule, which is in place since 2012, is applying an abuse assumption in a rather general manner. We estimate that there are good chances that the new rule is also contrary to European Law. As mentioned earlier, the European Court of Justice has already a case on this rule to judge. Therefore, we recommend not to accept denials of withholding tax refunds according to Section 50d (3) German Income Tax Act also for fiscal years since 2012. Second, as the old and the new German anti-abuse rules of Section 50 d (3) German Income Tax Act have no limitation on shareholding quotas, the free movement of capital could also be pertinent, and not the freedom of establishment (i.e. if the shareholding quota of the holding company is so low that the holding company has no substantial influence on the subsidiary). This would bring also portfolio interest holding companies of non-EU member countries in a position to contest the denial of the capital tax refund as it is likely that the German anti-abuse rule also violates the free movement of capital.

We are happy to assist you on this matter. Please feel free to contact us.

be in touch: Any questions? Please do not hesitate to contact us!

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