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# EU Direct Tax Newsalert

## Dutch dividend refund claims by non-resident investment regimes subject to condition of substitution payment

On 23 October 2020, the Dutch Supreme Court (hereafter: "Supreme Court") published its long-awaited response to the prejudicial questions raised by the Court of Zeeland-West Brabant in the *Köln-Aktiefonds Deka* ("Deka") case. This response is a continuation of the referred questions to the European Court of Justice ("CJEU") regarding the refund of Dutch dividend withholding tax to foreign investment funds (C-156/17; see also our EUDTG Newsalert of 31 January 2020).

The referred questions concerned the compatibility of the Dutch Fiscal Investment Institution (FII) regime (as it read until 2007) with EU law, and, more specifically, the compatibility with EU law of applying the shareholder and distribution requirements to foreign investment funds when determining their entitlement to a refund of Dutch dividend withholding tax.

### Objectively comparable situation

The Supreme Court reconsiders its earlier judgment of 10 July 2015 in which it ruled that a non-resident investment fund is not comparable to a Dutch FII because it is not subject to Dutch dividend withholding obligation. Pursuant to the CJEU Judgement in the *Fidelity Funds* case (C-480/16), the Supreme Court considers that, since the Netherlands levies a dividend withholding tax on distributions both to resident and non-resident investment funds, it should ensure that non-resident investment funds are allowed access to the same systems that prevent double taxation for resident investment funds.

The Supreme Court states that not allowing the non-resident investment funds access to the refund of Dutch dividend withholding tax constitutes an obstacle to the free movement of capital which cannot be justified by compelling reasons of public interest. However, the Supreme Court considers that for the eligibility of a refund, a substitution payment is necessary, more on that below.

### Substitution payment

According to the Supreme Court, a non-resident investment fund which meets the FII-conditions can apply for a refund which is determined by taking into account a voluntary payment of Dutch dividend withholding tax on its distributions (the so-called "substitution payment"). A successful claim for a refund therefore can only be made when the condition of the substitution payment is met.

The substitution payment is based on the amount of Dutch dividend withholding tax that

would have been withheld from the distributed profits if the non-resident investment fund and its shareholders would have resided in the Netherlands. Dividend taxes suffered are then deducted from this amount. If the calculation results in a negative amount, the substitution payment is set at nil. A refund is only granted to the extent that the amount of tax withheld from the dividends received by the non-resident investment fund exceeds the substitution payment.

With regard to the compatibility with EU law of the shareholder and distribution requirements, the Supreme Court states that this only becomes relevant when the non-resident investment fund agrees to the substitution payment.

### Shareholders requirement

A non-resident fund that agrees to the substitution payment, must demonstrate that it meets the shareholder requirements. If this cannot be substantiated by the non-resident investment fund, it cannot be considered comparable to a Dutch FII.

With regard to the question whether the shareholder requirements lead to a *de facto* discriminatory treatment of non-resident investment funds, the Supreme Court finds that the listing requirement on the Amsterdam stock exchange is more burdensome for non-resident investment funds. This requirement was in force in the period 2002 – 31 July 2007 after which the regime was modified. With the entry into force of the modified regime in 2007, the Supreme Court considers that this obstacle has been removed. In the view of the Supreme Court, the modified regime applies indiscriminately and does not constitute a restriction on the free movement of capital. The Supreme Court therefore considers that application of the modified regime to cases in the period 2002 – 31 July 2007, to be sufficient to remedy the discriminatory treatment.

### Distribution requirements

The Supreme Court considers that the main objective of the FII regime lies in the taxation of profits of the shareholders in an investment fund. As stated by the CJEU, it follows that a resident investment fund which makes an actual distribution of its profits, and a non-resident investment fund whose profits are not distributed but are deemed to have been distributed and are taxed as such at the level of the shareholders in that fund, must be regarded as being in objectively comparable situations.



The Supreme Court considers that in such a situation, a refusal to grant a refund to the non-resident investment fund would constitute a restriction on the free movement of capital which cannot be justified.

The Supreme Court further considers that the distribution requirement is met if the profit available for distribution is actually distributed to the shareholders of the investment fund within eight months after the end of the (financial) year, regardless whether there is a legal or statutory requirement to do so.

### **Takeaway**

Although non-resident investment funds may be considered comparable to a Dutch FII, the introduction of the “substitution payment” as condition that should be fulfilled in order for the funds to obtain a refund, will limit the possibility of a refund claim. In case the amount of tax withheld from the dividends received by non-resident investment funds is the same or higher than the amount of the substitution payment this likely does not result in a refund. We will therefore further analyse the impact of this Supreme Court decision for pending claims.

Furthermore, we will await the final outcome of this case since the judgment of the Supreme Court was a reply on preliminary questions raised by the lower court. The lower court has to make a decision on the claims filed in accordance with the judgment of the Supreme Court.