

Amurta: A Tribute to (the Late) Advocate General Geelhoed

1. Introduction

On 8 November 2007, the European Court of Justice (ECJ) delivered its decision in the *Amurta* case,¹ which addresses economic double taxation on cross-border profit distributions within the European Union. The case draws on the legacy of the Opinions of Advocate General Geelhoed, wherein he has developed a highly relevant framework for deciding individual cases in this area. This article, following a summary of Geelhoed's thoughts, discusses the *Amurta* case and its implications.

2. Geelhoed's Lessons

On 14 December 2006, Prof. Geelhoed lectured at a combined gathering of two professional associations in Amsterdam.² Briefly, after his lecture he fell ill and passed away on 20 April 2007. Geelhoed, who had just retired as Advocate General, spoke freely about his views on the ECJ's case law in the area of direct taxation. The following provides a brief summary of his lecture, which emphasized the obstacles that the ECJ encounters in giving decisions in this area, such as in the *Amurta* case.

At the outset, Geelhoed criticized the ECJ's standard observation in tax cases that, although taxation falls within the competence of Member States, they must nonetheless exercise that competence consistently with Community law. The pitfall of this observation is that it does not provide an answer to the central question as to whether or not Community law is fit to apply equally to the various areas of law that fall under the scope of the EC Treaty. In Geelhoed's view, it makes a difference whether the Community law at issue applies to quality prescriptions for the import of products, to conditions for the accession to a profession, or to the attribution of the authority to levy direct taxes. Geelhoed's view is not motivated by a bias in favour of the concept of tax sovereignty of Member States. Rather, when it comes to sovereignty in the area of (direct) taxation, he believes that Member States only have conditional tax sovereignty, i.e. they only have a domestic legislative authority to the extent that the European Community has not exercised its own authority. The basis of Geelhoed's view that Community law cannot apply equally to direct taxes, but relates instead to the history and function of the fundamental freedoms of the EC Treaty.

Referring to the "iron age" of Community law, Geelhoed finds a distinction between distortions that originate from discriminatory rules under the domestic laws of Member States, and disparities that stem from the coexistence of different Member States' tax regimes.³ Based on the original language of the EC Treaty, it is evident

that the fundamental freedoms served to remove the former distortions, whereas Arts. 100, 101 and 102 served to remove disparities by means of harmonization. Arts. 101 and 102, in particular, were intended to address disparities of a fiscal nature. This rather clear distinction was distorted by the *Dassonville* case in 1974, which was followed by the *Cassis de Dijon* case in 1979.⁴ In these cases, the ECJ found a way to apply the fundamental freedoms to rules that were not discriminatory, but in fact represented disparities between the laws of the Member States. Insofar as the ECJ has also applied the fundamental freedoms to matters of direct taxation, Geelhoed strongly believes that this is inappropriate when it comes to disparities, i.e. distortions that stem from differences between the coexisting, non-harmonized tax laws of the Member States.

In elaborating on this theme, Geelhoed comes to the heart of the matter. Inevitably, when the ECJ has to deal with a distortion that is not caused by a single Member State, but rather two or even more Member States, such distortion or disparity cannot be resolved without the ECJ being engaged in the allocation or apportionment of powers of taxation between the Member States. When it comes to the allocation of taxing powers, this has to be done in a consistent, predictable way that offers legal certainty by means of a pre-defined fixed pattern on the basis of which future cases can be resolved. According to Geelhoed, the ECJ is not able to fulfil this role. The EC Treaty simply does not provide any guidance to the ECJ as how to allocate taxing powers between the Member States. Similarly, the ECJ's case law concerning the fundamental freedoms has not defined predictable criteria according to which tax disparities can be removed.

For instance, Geelhoed finds it unacceptable that the outcome of a case largely depends on whether it has

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1. ECJ, 8 November 2007, Case C-379/05, *Amurta SGPS v. Inspecteur van de Belastingdienst/Amsterdam*.

2. *Vereniging voor Belastingwetenschap* (a Netherlands association for tax professionals and academics) and the *Nederlandse Vereniging voor Europees Recht* (a Netherlands association for European law experts). Prof. F. Vanistendael and Prof. P. J. Wattel also lectured at this meeting. The lectures and the subsequent discussions were published (in Dutch) in, "De Soevereiniteit van de lidstaten van de Europese Unie op het terrein van de directe belastingen", *Geschriften van de Vereniging voor Belastingwetenschap*, No. 230, available at www.belastingwetenschap.nl.

3. Geelhoed referred, in this respect, to the report of the Intergovernmental Committee on European Integration, *The Brussels Report on the General Common Market*, June 1956, p. 21 (the Spaak report).

4. ECJ, 11 July 1974, Case 8/74, *Procureur du Roi v. Benoît and Gustave Dassonville* and ECJ, 20 February 1979, Case 120/78, *Rewe-Zentral AG v. Bundesmonopolverwaltung für Branntwein (Cassis de Dijon)*.

been referred to the ECJ by the source state or by the state of residence. In this respect he criticizes the *Bosal* case.⁵ If a similar case were to be submitted to the ECJ by the source state, the existing judgment in the *Bosal* case would not provide any guidance and the ECJ would again have to find a way to allocate the taxing powers in this situation. Geelhoed believes that the ECJ can only fulfil its role if a single Member State is to blame for the existence of a distortion. To the extent that two or more Member States are responsible for the distortions, it is impossible to resolve the issues within the existing *Dassonville* and *Cassis de Dijon* framework,⁶ and it makes no sense to hold a single Member State responsible for such a disparity. In this respect, Geelhoed classifies the *Manninen* case⁷ as “bad law”. He confessed that he had been intentionally silent concerning *Manninen* in his Opinion in the *Kerckhaert Morres* case.⁸ Reading between the lines, it can be interpreted that he attempted to circumvent the *Manninen* decision and encourage the ECJ to reach an opposite decision in *Kerckhaert Morres*. Although he partially succeeded, Geelhoed still found the ECJ judgment in *Kerckhaert Morres*⁹ extremely unsatisfactory, because it demonstrates that the outcome of a case depends, to a large extent, on the technical details of the disputed tax regime. In answer to a question from the audience,¹⁰ Geelhoed confirmed that if the Belgian levy would have been subject to a credit system (i.e. an offset of Belgian withholding tax against the personal income tax liability of the shareholder), it would probably have been more difficult to stay away from the line of reasoning in the *Manninen*,¹¹ *Lenz*¹² and *Verkooijen*¹³ cases.

This raises the issue as to whether the ECJ should become more progressive and define its own framework for the allocation of taxing powers between the Member States. Geelhoed does not advocate a pseudolegislatory role for the ECJ. In a typical “balance of powers” situation, a court can be very active in this respect, i.e. if there is a legislator that can overrule the court if it heads in the wrong direction. The EC legislator, however, is bound by the unanimous vote requirement of Art. 94 of the EC Treaty, which is a strong argument for judicial restraint on the part of the ECJ. Geelhoed never mentioned this, but he explained that this urged him to be very careful when developing his thoughts in his Opinions.

3. The ECJ and Apportionment of Fiscal Jurisdiction

3.1. Legal framework

Although not as outspoken as in his lecture on 14 December 2006, Geelhoed had already addressed these issues in his Opinions dealing with economic double taxation of companies and their shareholders with respect to distributions of company profits.¹⁴ In particular, with respect to shareholder relief from economic double taxation, the tax regimes of the Member States differ, resulting in disparities that can hardly be solved without touching upon the allocation of taxing powers between the Member States. Absent a harmonized sys-

tem for the avoidance of economic double taxation, the Member States apply different techniques and different sub-techniques, even within the same Member State for different classes of shareholders, to prevent or mitigate economic double taxation.¹⁵

3.2. Economic double taxation and the allocation of taxing powers

Depending on the technique at hand, relief from economic double taxation may take place at the level of the distributing company (corporate income tax, dividend withholding tax) or at the level of the shareholder (corporate or individual income tax). Obviously, and generally speaking, a Member State is more willing to provide relief to its domestic shareholders for corporate income tax that it has collected, than for corporate income tax collected by another Member State. We have seen examples of this in *Baars*, *Verkooijen*, *Lenz*, *Manninen*, *FII Group Litigation* and *Meilicke*.¹⁶ In addition, and again generally speaking, Member States that offer relief from economic double taxation at source (i.e. at the level of the distributing company) tend to be more generous in providing relief from economic double taxation on profits distributed by resident companies to resident shareholders as opposed to non-resident shareholders. Examples in this respect can be found in *Fokus Bank*, *Bouanich*, *ACT Group Litigation*, *Denkavit* and *Amurta*.¹⁷ The discrimination that follows from favourable treatment of domestic share investments and domestic shareholders results in distortions that can be removed with the aid of the fundamental freedoms of the EC treaty, as the above-mentioned cases have demonstrated (or of the EFTA agreement, in the case of *Fokus Bank*). Removing

5. ECJ, 18 September 2003, Case C-168/01, *Bosal Holding BV v. Staatssecretaris van Financiën*. Geelhoed criticized the *Bosal* judgment in ECJ, Advocate General Geelhoed's Opinion, 23 February 2006, Case C-374/04, *Test Claimants in Class IV of the ACT Group Litigation v. Commissioners of Inland Revenue*, Paras. 62-64.

6. See note 4.

7. ECJ, 7 September 2004, Case C-319/02, *Petri Manninen*.

8. ECJ, Advocate General Geelhoed's Opinion, 6 April 2006, Case C-513/04, *Mark Kerckhaert, Bernadette Morres v. Belgian State*.

9. ECJ, 14 November 2006, Case C-513/04, *Mark Kerckhaert, Bernadette Morres v. Belgian State*.

10. The question was asked by Dr O.C.R. Marres.

11. See note 7.

12. ECJ, 15 July 2004, Case C-315/02, *Anneliese Lenz v. Finanzlandesdirektion für Tirol*.

13. ECJ, 6 June 2000, Case C-35/98, *Staatssecretaris van Financiën v. B.G.M. Verkooijen*.

14. See *ACT Group Litigation*, note 5; ECJ, Advocate General Geelhoed's Opinion, 6 April 2006, Case C-446/04, *FII Group Litigation v. Commissioners of Inland Revenue*; and ECJ, Advocate General Geelhoed's Opinion, 27 April 2006, Case C-170/05, *Denkavit*.

15. See Geelhoed's overview of the existing systems of shareholder relief in his Opinion in the *ACT Group Litigation* case, note 5, Paras. 4-7.

16. ECJ, 13 April 2000, Case C-251/98, *C. Baars v. Inspecteur der Belastingdienst Particulieren/Ondernemingen Gorinchem*; *Verkooijen*, note 13; *Lenz*, note 12; *Manninen*, note 7; ECJ, 12 December 2006, Case C-446/04, *FII Group Litigation*; and ECJ, 6 March 2007, Case C-292/04, *Wienand Meilicke*.

17. EFTA Court, 23 November 2004, Case E-1/04, *Fokus Bank*; ECJ, 19 January 2006, Case C-265/04, *Bouanich*; ECJ, 12 December 2006, Case C-374/04, *Test Claimants in Class IV of the ACT Group Litigation v. Commissioners of Inland Revenue*; ECJ, 14 December 2006, Case C-170/05, *Denkavit Internationaal BV, Denkavit France SARL v. Ministre de l'Économie, des Finances et de l'Industrie*; and *Amurta*, see note 1.

discriminatory elements on a case-by-case basis does not, however, result in a harmonized system for the relief from economic double taxation on profit distributions. It may result in shareholder relief in the source state or in the home state, or may not result in relief from economic double taxation at all. In the *Kerckhaert Morres* case, the ECJ went so far as to accept that the combination of the French and Belgian tax regimes resulted in economic and juridical double taxation of the dividend flows. And as we have learned from the ECJ, the existence of economic double taxation as such (as is the case with respect to juridical double taxation) that results “from the exercise in parallel by two Member States of their fiscal sovereignty” is not in breach of Community law.¹⁸

When it comes to applying the fundamental freedoms to the domestic regimes for relief from economic double taxation, the fragmented outcome of this “negative integration” results, in some cases, in a shift of the tax base from the source state to the home state (for example *Fokus Bank*, possibly *Bouanich*, and possibly *Amurta*), and in other cases in a reduction of the tax base in the home state of the shareholder in favour of the taxing power of the source state (for example *Lenz*, *Manninen*, *Meilicke*). If one were to design an overall system for relief from economic double taxation, the first and most obvious question would be whether the source state (the residence state of the company distributing the profits) would have priority over the taxing rights of the home state (the country of residence of the shareholder), or the other way around, or whether it would be possible to design a mechanism of shared taxing powers in this respect, similar to the allocation of fiscal jurisdiction between home state and source state with respect to dividend income in tax treaties. Obviously, one should be aware that tax treaty provisions similar to Art. 10 of the OECD Model Convention (hereinafter: the OECD Model) divide the taxing powers with respect to dividend income between the source and the home state in order to avoid juridical double taxation on dividend income in the hands of the shareholder, whereas the issue at hand is the avoidance of economic double taxation.

Relief from economic double taxation with respect to dividend income is generally not addressed in tax treaties. Therefore, there is no internationally accepted framework available (such as tax treaties that are in line with the OECD Model)¹⁹ to which the ECJ could refer if it were to design a system of cross-border relief from economic double taxation. This means that the ECJ would have to make its own choices with respect to the allocation of taxing powers (i.e. to the state of the company, to the state of the shareholder, or to both, in part). It would be extremely difficult for the ECJ to make such choices without having any external or authoritative guidance that it could rely on (although it should be noted that the ECJ has already carefully begun to distinguish between home state and source state obligations, and in a way has implied that the home state is in the best position to provide relief from economic double taxation).²⁰

The ECJ has already decided not to interfere with the allocation of taxing powers agreed upon in the Member States’ tax treaties²¹ with respect to juridical double taxation. It can be concluded, which is in line with Geelhoed’s observations, that the ECJ cannot do anything other than remove, on a case-by-case basis, discriminatory elements of domestic regimes that relate to economic double taxation of dividend flows and the shareholder relief provided for in these situations. Inevitably, the technical design of these regimes, in order not to discriminate against foreign shareholders and/or shareholdings in foreign companies, will be of more importance than whether these regimes result in a balanced overall treatment of cross-border investments, as was evidenced by the ECJ’s decision in the *Kerckhaert Morres* case.

4. The *Amurta* Case

4.1. Introductory remarks

Following the ECJ’s decision in *Denkavit*, the outcome of the *Amurta* case, on 8 November 2007, did not come as a surprise. In brief, the ECJ ruled that the Netherlands dividend withholding tax exemption that applied to resident shareholders owning a qualifying shareholding in a resident subsidiary, should also be granted to non-resident shareholders owning a similar shareholding in a resident subsidiary. In *Denkavit*, the ECJ had already ruled that a French withholding tax exemption applicable to French parent companies owning shares in a resident subsidiary should also be extended to a Netherlands parent company owning shares in a resident subsidiary. The relatively new elements in the *Amurta* case relate to the role of a tax treaty between the home state of the shareholder and the profit distributing company’s state, and to the (ir)relevance of unilateral relief provided to the shareholder in the home state.

4.2. The facts

Amurta SGPS, a Portuguese company, held 14% of the shares in Retail BV, a Netherlands company. The shareholding fell outside the scope of the EC Parent-Subsidiary Directive,²² which required a minimum shareholding of 25% at that time. On 31 December 2002 Retail BV withheld 25% Netherlands dividend withholding tax (i.e. the statutory withholding tax rate) on dividends paid to *Amurta*. However, on dividends paid to its Netherlands corporate shareholder, Sonaetelecom BV, which owned 66% of the shares, it applied the exemption found in Art. 4 of the Netherlands Dividend

18. *Kerckhaert Morres*, note 9, Para. 20.

19. See ECJ, 12 May 1998, Case C-336/96, *Mr and Mrs Robert Gilly v. Directeur des services fiscaux du Bas-Rhin*, Para. 31.

20. See *ACT Group Litigation*, note 17, Paras. 58-60.

21. See Gilly, note 19, Paras. 23-31; ECJ 5 July 2005, Case C-376/03, *D. v. Inspecteur van de Belastingdienst/Particulieren/Ondernemingen buitenland te Heerlen*, Paras. 49-52; *Kerckhaert Morres*, note 9, Para. 22; ECJ, Advocate General Bot’s Opinion, 3 July 2007, Case C-194/06, *Orange European Small Cap Fund*, Paras. 48-49.

22. 90/435/EEC.

Withholding Tax Act (DWTA). Under the Netherlands–Portugal tax treaty, the Netherlands was allowed to levy a 10% dividend withholding tax, which means that Amurta was entitled to a refund of 15%. Nevertheless, Amurta claimed a refund of the full 25% from the Netherlands tax authorities, arguing that it was entitled to an exemption from withholding tax similar to the exemption that applied to the Netherlands corporate shareholder Sonaetelecom BV.

4.3. Legal background

The dividend withholding tax exemption of Art. 4 of the DWTA relates to the participation exemption regime under the Netherlands Corporate Income Tax Act (CITA). The Netherlands applies the ‘classical system’ to company profit distributions, which means that a company is subject to corporate income tax on its profits, and the individual shareholder is separately taxed on the dividend income that it receives from the company. Although it is intended that this classical system will result in economic double taxation (i.e. of corporate income tax at the level of the company and personal income tax at the level of the shareholder) with respect to individual shareholders, economic double taxation is undesirable with respect to dividends paid to corporate shareholders. Therefore, Netherlands parent companies (and Netherlands permanent establishments of non-resident parent companies) are allowed to receive dividends exempt from corporate income tax under the participation exemption regime of Art. 13 of the CITA, provided that the shareholding in the subsidiary meets certain requirements (“qualifying shareholding”). One of these requirements is a minimum shareholding of 5%. Without the Art. 4 DWTA exemption, a Netherlands parent company that receives a dividend from a qualifying shareholding in a Netherlands subsidiary that has been subject to dividend withholding tax, would either be entitled to a credit of such dividend withholding tax against corporate income tax on its other (taxable) income, or, to the extent that it does not have such tax capacity related to other income, it would be entitled to a refund of the Netherlands withholding tax paid on its exempt dividend income. In other words, the Netherlands parent company would be entitled to a “full credit”, which includes a cash refund of any excess credit. Given this background, it does not make sense to levy Netherlands dividend withholding tax on a dividend paid to a Netherlands corporate shareholder that benefits from the participation exemption. Such dividend withholding tax would have to be credited or, in most cases, refunded, in any event. Based on these administrative concerns Art. 4 of the DWTA provided for a dividend withholding tax exemption for dividends paid to a parent company that benefited from the participation exemption for its (qualifying) shareholding in the distributing company. As mentioned above, only Netherlands resident companies²³ can benefit from the participation exemption. As a result, the withholding tax exemption of Art. 4 of the DWTA only applied to dividends paid to Netherlands parent companies and not to non-resident parent companies.²⁴

4.4. Questions referred to the ECJ for a preliminary ruling

The Court of Appeals of Amsterdam referred the following questions to the ECJ for a preliminary ruling:

1. Is the exemption under Article 4 [DWTA] (...) contrary to the provisions on the free movement of capital (Articles 56 EC to 58 EC), given that the exemption is applicable only to dividend payments to shareholders liable to corporation tax in the Netherlands (...) ²⁵ to whom the shareholding exemption under Article 13 [CITA] (...) applies?
2. Does the answer to the (preceding) question depend on whether the State of residence of a foreign shareholder/company to which the exemption under Article 4 [DWTA] (...) does not apply grants that shareholder/company full credit for Netherlands dividend tax?”

Clearly, the second question served to determine whether the discrimination of foreign corporate shareholders embedded in the Netherlands withholding tax exemption of Art. 4 of the DWTA could be neutralized by way of a credit for this discriminatory tax in Portugal, the home state of Amurta. Assuming that Portugal would allow a full credit for this Netherlands dividend tax, this dividend tax would not result in an increase in the overall effective tax burden for Amurta. The only result of the dividend tax levied by the Netherlands would be a shift of taxing powers from Portugal to the Netherlands because the Netherlands dividend tax would reduce the tax paid by Amurta in Portugal. Such an apportionment of fiscal jurisdiction was, however, agreed upon in Arts. 10 and 24 of the Netherlands–Portugal tax treaty. Therefore, this shared allocation of taxing powers, as such, could not be contrary to Community law. In other words, if Amurta received a full credit for the Netherlands dividend tax against its tax liability in Portugal, it would be questionable whether or not the Netherlands dividend tax would still be deemed to constitute a restriction on Amurta’s freedom to invest in a Netherlands company, such as Retail BV.

4.5. The decision of the ECJ

4.5.1. First Question

4.5.1.1. Primary versus secondary EC law

To a large extent the ECJ followed the reasoning of Advocate General Mengozzi.²⁶ According to the ECJ, the Netherlands withholding tax regime constitutes a restriction on the free movement of capital by treating dividends paid to companies established in another Member State less favourably than dividends paid to companies established in the Netherlands. For shareholdings that fall outside the scope of the Parent-Sub-

23. And Netherlands permanent establishments (PEs) of non-resident companies.

24. With the exception of non-resident companies having a PE in the Netherlands to which the shares in the Netherlands subsidiary were attributable, which, however, seldom occurred.

25. The deleted part relates to the PE situation, which is not directly relevant in the *Amurta* case.

26. ECJ, Advocate General Mengozzi’s Opinion, 7 June 2007, Case C-379/05, *Amurta*.

subsidiary Directive, the Member States can unilaterally determine whether and how to prevent economic double taxation on dividend payments. However, the fact that Amurta's shareholding in Retail BV fell outside the scope of the Parent-Subsidiary Directive, "does not of itself mean that the Member States are entitled to impose measures that contravene the freedoms of movement guaranteed by the EC Treaty".²⁷

4.5.1.2. Non-resident shareholder in a comparable situation?

In reviewing the justifications for this restriction,²⁸ the ECJ held that there is no objective difference between a non-resident shareholder receiving dividends from a Netherlands company and a resident shareholder, given the fact that these two categories are equally subject to Netherlands dividend withholding tax.²⁹ Also, the fact that Amurta was not subject to Netherlands corporate income tax (as opposed to Sonaetelecom BV), and, therefore, could not avail itself of the participation exemption regime to which the exemption in Art. 4 of the DWTA was directly linked, was not accepted as an argument in favour of concluding that Amurta's position was not comparable to that of a Netherlands parent company.

4.5.1.3. Distortion or disparity?

The ECJ also addressed the issue of whether or not the case at hand resulted in a disparity stemming from the co-existence of two Member States' tax regimes or a distortion that could be addressed by the fundamental freedoms of the EC Treaty. The ECJ observed that the economic double taxation of the dividends paid to Amurta stems solely from the exercise by the Netherlands of its taxing powers. In other words, only the Netherlands is to blame for the fact that economic double taxation occurred with respect to the dividends paid to Amurta in contrast to dividends paid to a Netherlands parent company, which are not subject to such double taxation. And, as we learned from Geelhoed, if only one Member State is to blame, there is no reason for judicial restraint by the ECJ. Obviously, if income tax is levied on Amurta's dividend income by Portugal, this would also result in economic double taxation; however, neither the Netherlands nor Portugal would be solely to blame for such economic double taxation. As we have seen, this would be a disparity which the ECJ could not address, which explains why the ECJ only focuses on the double tax consequences of the Netherlands withholding tax regime in this respect.

4.5.1.4. Fiscal cohesion

Finally, and still in light of the first question, the ECJ dealt with the argument of fiscal cohesion, including the need to safeguard the balanced allocation of the power to tax between the Member States. The ECJ ruled simply that, in a situation where the Netherlands has chosen not to tax resident (corporate) shareholders, they cannot rely on the argument of fiscal cohesion to justify the taxation of non-resident corporate shareholders. Therefore, it

concluded that the Netherlands withholding tax regime at hand was contrary to the freedom of capital.

4.5.2. Second Question

4.5.2.1. Unilateral relief in Portugal

The second question referred to the ECJ was based on the assumption that the Netherlands dividend withholding tax could be fully credited against Amurta's corporate income tax liability in Portugal. However, Amurta contested that it was entitled to such a tax credit, and pointed out that it benefited from a participation exemption regime in Portugal. And although Amurta was entitled to a tax credit for Netherlands dividend withholding tax under the tax treaty with Portugal, this credit was limited to the amount of Portuguese tax attributable to the dividends, which was zero according to Amurta. The ECJ made it clear that it was not competent to determine whether or not Amurta was entitled to a tax credit in Portugal. Even if Amurta was entitled to a credit against Portuguese tax, it ruled that "it is settled case-law that unfavourable tax treatment contrary to a fundamental freedom cannot be justified by the existence of other tax advantages, even supposing that such advantages exist", that "the Kingdom of the Netherlands is under a duty to ensure that (...) recipient companies established in another Member State are subject to the same treatment as recipient companies established in the Netherlands" and that, accordingly, "the Netherlands cannot rely on the existence of a tax advantage granted unilaterally by another Member State in order to escape its obligations under the Treaty".³⁰ To this extent the ECJ confirmed the reasoning of the EFTA Court in *Fokus Bank*, Para. 37, which, in the author's view, boils down to the argument that advantages of an arbitrary nature, that arise outside the jurisdictional scope of the Member State that is responsible for the restriction, cannot neutralize such a restriction. The ECJ did not, however, follow the EFTA Court in its observations that an unfavourable treatment cannot be neutralized by means of a tax treaty,³¹ which seems to relate to the fact that the contents of a tax treaty fall within the jurisdictional scope of the Member State that is responsible for the dis-

27. *Amurta*, note 1, Para. 24. The ECJ had already mentioned this in the *ACT Group Litigation* case, note 17, Para. 54.

28. In particular those of Art. 58(1)(a) of the EC Treaty, which allow differential treatment on the basis of residence.

29. This argument can be traced back as far as the *Avoir fiscal* case: ECJ, 28 January 1986, Case 270/83, *Commission of the European Communities v. French Republic (Avoir fiscal)*, Paras. 19-20, but sometimes tends towards circular reasoning: the discrimination at hand stems from imposing a higher tax burden on non-residents than the burden on residents, which is only possible if non-residents are also subject to tax. But by making these non-residents subject to tax, they become comparable to residents. In other words, it has become quite difficult for a Member State to do what is explicitly allowed by Art. 58(1)(a) of the EC Treaty, i.e. to distinguish between resident and non-resident taxpayers, in particular when these taxpayers are shareholders subject to dividend withholding tax. Perhaps the difference between resident and non-resident shareholders can still be used to justify taxation of non-resident shareholders on the basis of gross dividend payments, as opposed to a final taxation on the basis of net income for resident shareholders.

30. *Amurta*, note 1, Paras. 75-78.

31. See *Fokus Bank*, note 17, Para. 38.

tortion and, therefore, can be seen as forming part of the legal framework of that very Member State.

4.5.2.2. Relief under the tax treaty

In *Bouanich*, the ECJ had already confirmed that a tax treaty may form part of the legal background of the case, and that a tax treaty should be taken into account in interpreting Community law.³² More precisely, in order to determine whether a non-resident shareholder is treated less favourably than a resident shareholder, in addition to taking into account national laws, the advantages of a tax treaty that the non-resident shareholder may benefit from, should also be considered.³³ In his Opinions in the *ACT Group Litigation* case³⁴ and in *Denkavit*, Geelhoed observed that the combination of home state and source state obligations under the free movement provisions should be viewed as a whole. Examining a case only from the perspective of one state, without taking into account the obligations of the other state under the EC Treaty, would give an unbalanced and misleading impression, and would not capture the economic reality of the case at hand.³⁵ Geelhoed's reasoning did not, however, extend to the point of accepting that unilateral relief provided for in the home state can neutralize a restriction of one of the freedoms in the source state. Rather, given the freedom of the Member States to define their own criteria for allocating taxing powers and to apportion taxing jurisdiction between themselves, Geelhoed concludes that a Member State should be allowed "to ensure the fulfilment of its obligations under the Treaty free movement provisions by means of provisions contained in a DTC", which means that it is open to a "source State which imposes double economic taxation on dividends to ensure, by a tax treaty and following interstate negotiations, that this will be relieved by the home state."³⁶ The ECJ seemed to have accepted his line of reasoning in the *ACT Group Litigation* case, in *Denkavit*, and also in the *Thin Cap Group Litigation* case,³⁷ although, in the end, it was not held in any of these cases that under the applicable tax treaty a discriminatory regime in the source state was effectively neutralized by the home state.

In *Amurta*, the referring Netherlands court did not make any reference to the tax treaty between the Netherlands and Portugal, and, therefore, the ECJ lacked information about the relevant provisions and about their impact (if any) on the tax treatment of *Amurta* in Portugal with respect to the Netherlands withholding tax. It decided that it is for the national court to establish whether it should take the tax treaty into account and, if so, whether the tax treaty effectively neutralized the restriction of the free movement of capital caused by Art. 4 of the DWTa in the Netherlands.³⁸ Although the ECJ explicitly accepts that the tax treatment under the tax treaty is capable of neutralizing the discrimination in the Netherlands, the chances that this is the case are fairly low. In his Opinion, Advocate General Mengozzi had already indicated that under the tax treaty, Portugal would only provide an "ordinary" or "partial" credit for

Netherlands dividend withholding tax up to the level of Portuguese tax attributable to the dividend income, whereas a Netherlands shareholder would benefit from a "full" credit in the Netherlands, thus leaving the non-resident shareholder in a less favourable position compared to a resident shareholder.³⁹ It is not clear what Mengozzi meant by a "full" credit, but it is possible that even if Portugal would allow a carry-forward of any excess credit, this would not match the situation of an exempt Netherlands shareholder. Such equal treatment would only exist if Portugal was obliged, under the treaty, to actually refund, in cash, the Netherlands withholding tax to the extent that it cannot be credited against Portuguese tax (i.e. an excess credit). Obviously, such a cash refund by the home state, of withholding tax levied in the source state, is not internationally accepted in the tax practice of the Member States, nor does the EC Treaty require a home state to pay such a refund.⁴⁰ Therefore, it is hardly to be expected that any existing tax treaty will be able to neutralize such a discriminatory levy of withholding tax in the source state.

5. The Consequences of the *Amurta* Case

5.1. Other alternatives

As mentioned above, it would be difficult to provide domestic shareholders with an exemption from withholding tax, on the one hand, and to ensure by means of a tax treaty that the levy of withholding tax from non-resident shareholders is fully neutralized by the home state, on the other hand. In this respect, it is unlikely that the alternative developed by Geelhoed is of any practical relevance, other than incidentally in situations such as *Bouanich*, where the repurchase of shares from non-resident shareholders was treated differently under a tax treaty than under national law.

This raises the issue as to what Member States should do if they want to continue to levy dividend withholding tax but at the same time want to prevent or mitigate economic double taxation of dividends, or, as the case may

32. See *Bouanich*, note 17, Para. 51.

33. *Id.*, Paras. 55-56.

34. See Advocate General Geelhoed's Opinion in *ACT Group Litigation*, note 5.

35. See Advocate General Geelhoed's Opinion in *Denkavit*, note 14, Para. 37.

36. Geelhoed, in his opinion in *Denkavit*, note 14, Paras. 35 and 40. Geelhoed made this conclusion subject to the condition that the actual effect of the treatment of a non-resident shareholder under the tax treaty must be equivalent to that of a resident shareholder, and that the source state continues to be responsible to ensure that the home state fulfils its obligations under the tax treaty to neutralize the - in principle - discriminatory rules of the source state.

37. See *ACT Group Litigation*, note 17, Para. 71; *Denkavit*, note 17, Para. 45; ECJ, 13 March 2007, Case C-524/04, *Test Claimants in the Thin Cap Group Litigation v. Commissioners of Inland Revenue*, Para. 54.

38. See *Amurta*, note 1, Para. 83.

39. See *Amurta*, note 26, Para. 88.

40. See *FII Group Litigation*, note 16, Paras. 50-57. A case is pending in the Netherlands where the taxpayer is claiming a refund of foreign withholding taxes to the extent that these cannot be credited against Netherlands tax (ref. Court of Appeals of The Hague, 29 August 2006, Case No. 04/01832, and the opinion of AG Wattel for the Supreme Court, 6 September 2007, Case No. 43.631).

be, of dividends that are paid to resident corporate shareholders. The introduction of a schedular tax in the form of a final levy on dividends, such as in Belgium, has proven to be in compliance with the EC Treaty (*Kerckhaert Morres*), but this system, by definition, will add to the series of tax charges imposed on distributed profits and, therefore, will not prevent economic double taxation of dividends paid to parent companies. Perhaps a system could be developed where the source state would assume the obligation (either unilaterally or under a tax treaty) to refund any withholding tax that cannot be credited in the home state. Whether or not and to what extent the home state grants a credit, and whether the home state grants this credit unilaterally or under a tax treaty with the source state, would be irrelevant under this system, because, in the end, the restriction on the freedom of movement would always be neutralized, either by the home state (credit), by the source state (refund), or by a combination of both (ordinary credit and refund of excess credit).

5.2. Non-differential withholding tax

Another alternative would be for the source state to levy dividend withholding tax equally from resident and non-resident shareholders, and to provide a credit (or a cash refund of any excess credit) for this withholding tax to resident shareholders that are subject to income tax levied in the source state or that are exempt from that tax. The fact that non-resident shareholders, in general,⁴¹ are not entitled to such a tax credit would be justified by the fact that these non-resident shareholders are not subject to income tax on these dividends in the Member State of the distributing company. Accordingly, non-resident shareholders (in respect of which the source state does not exercise its tax jurisdiction insofar as income tax is concerned) and resident shareholders would not be in an objectively comparable situation in this circumstance, and, therefore, equal treatment by the source state of these two categories would not be required. This line of reasoning is very close to the one accepted by the ECJ in the *ACT Group Litigation* case,⁴² in which the ECJ held that a source state's obligations are different from those of a home state when it comes to preventing economic double taxation on profit distributions.⁴³ Moreover, the idea that a technical amendment could be sufficient to turn a tax levy that is, in substance, discriminatory into a tax regime that is compliant with EC law, was accepted, albeit reluctantly, by Geelhoed in his lecture on 14 December 2006. In fact, the obligation to prevent economic double taxation would, in this situation, fall outside the scope of the tax jurisdiction of the source state. In this situation, whether or not there is any mitigation of economic double taxation,⁴⁴ would automatically become a matter to be dealt with by the home state, which, by definition, is in a position to determine the final tax due on the dividend income and to grant a credit against this final tax liability for source state taxes.⁴⁵

5.3. Equal treatment of excess credits

The drawback for a Member State adopting this alternative is that, although the Member State would be in compliance with Community law as a source state, it would also have to be in compliance with Community law when it operates as a home state. If it provides a credit, or even refund, of domestic withholding tax for domestic shareholders, the question arises as to whether these domestic shareholders should also be entitled to a credit, or – more importantly – a refund, of foreign withholding tax, based on the *Lenz*, *Manninen* and *Meilicke* cases. Although a Member State is not obliged to prevent juridical double taxation,⁴⁶ when it avoids juridical double taxation of domestic dividends, it should provide equal treatment to dividends received from non-resident companies.⁴⁷ The ECJ has held, however, that when it comes to offsetting foreign withholding tax against an income tax liability in the home state of the shareholder, such credit only has to be granted “up to the limit of the amount of corporation tax for which the company receiving the dividends is liable.”⁴⁸ In other words, if the source state applies “a higher level of tax” than the home state (i.e. in the event of an excess credit), the latter “is not required to repay the difference, that is to say, the amount paid in the Member State of the company making the distribution which is greater than the amount of tax payable in the Member State of the company receiving it.”⁴⁹ Geelhoed had already pointed out that such a difference in levels of taxation in fact represents “a disparity between national tax systems, with which Article 43 EC is not concerned.”⁵⁰ Advocate General Bot also recently excluded a Portuguese withholding tax of 17.5% from EC Treaty protection to the extent that it exceeded the Netherlands tax related to the dividends of 15%.⁵¹ Similar conclusions can be drawn from the *Gilly* case, in

41. In some situations non-resident shareholders are liable to income tax for the dividends received and will thus also be able to credit the withholding tax on these dividends, for instance in the event of a domestic PE to which the dividend income is attributable.

42. See *ACT Group Litigation*, note 17, Paras. 47-74.

43. *Id.*, Paras. 58-60. Geelhoed had already extensively analysed these differences between home state and source state obligations in his Opinion in the *ACT Group Litigation* case, note 5, Paras. 58-73.

44. It should be borne in mind that the EC Treaty does not oblige Member States to avoid economic double taxation in situations not covered by the Parent-Subsidiary Directive; see *Amurta*, note 1, Para. 24.

45. This would be in line with the ECJ's observation in *ACT Group Litigation* (see note 17, Para. 60), that the home state is best placed to determine the shareholder's ability to pay tax, which implies that it is primarily an obligation of the home state to provide for relief from economic double taxation, if read in conjunction with the Court's observation in Para. 59 that the Member State in which the company making the distribution is resident cannot reasonably be expected to refrain from taxing the company's profits, because that would effectively oblige this Member State to “abandon its right to tax a profit generated through an economic activity undertaken on its territory”.

46. *Kerckhaert Morres*, note 9, Para. 22 and Geelhoed in his Opinion in *Kerckhaert Morres*, note 8, Paras. 31-36.

47. See Geelhoed's Opinion in *Kerckhaert Morres*, note 8, Para. 19, albeit in respect of economic double taxation.

48. See *FII Group Litigation*, note 16, Para. 52.

49. *Id.*

50. Opinion in *FII Group Litigation*, note 14, Para. 45.

51. Opinion in *Orange European Small Cap Fund*, note 21, Paras. 139-144, and, in particular, in footnote 34.

which France was not obliged to refund German tax to the extent that it exceeded French tax.⁵² In situations where the statutory tax rates of the two Member States differ, a disparity exists that cannot be resolved by applying the fundamental freedoms of the EC Treaty. Excess credits are often, however, the result of the withholding tax being applied on a gross payment, whereas income tax in the hands of the shareholder is levied on a net base, i.e. after deducting costs and taking into account losses from other operations that are included in the worldwide tax base of the shareholder in his home state. Therefore, if the foreign withholding tax rate does not exceed the home state's statutory tax rate, the problem may also arise that foreign withholding taxes are not, or not fully, creditable. Although the difference in determining the withholding tax base in the source state, as opposed to an income tax base in the home state, can be considered as a disparity between the home and the source state,⁵³ such a difference becomes a distortion for which one state (the home state) is to blame, if this home state also neutralizes the difference between the (gross) withholding tax base and the (net) income tax base in a purely domestic situation. If the home state of the shareholder acknowledges that the effective level of income tax, due to the net basis of calculating the amount of taxable income, may be below the level of withholding tax on the gross payments, and for this reason provides for a refund of (excess, i.e. non-creditable) domestic withholding tax that was levied at source, it can be argued that this state would also be obliged to refund foreign withholding tax that cannot be credited for this same reason. The ECJ has also held, when discussing the differences between source state and home state obligations with respect to preventing or mitigating economic double taxation, that it is usually the home state of the shareholder "that is best placed to determine the shareholder's ability to pay tax" and that likewise the Parent-Subsidiary Directive "requires the Member State of the parent company which receives profits distributed by a subsidiary which is resident in another Member State, and not the latter State, to avoid a series of charges to tax, either by refraining from taxing such profits or by [providing for a tax credit for corporation tax and, if any, withholding tax levied in the other Member State]."⁵⁴ Therefore, as long as source states are allowed to levy withholding taxes on the basis of a gross payment, it can be argued that the home states that pay out a refund for domestic excess credits are also obliged to neutralize the difference between a foreign withholding tax and the lower tax liability on the basis of a net tax base with respect to the dividend income. This conclusion does not necessarily mean that the home state should also carry the budgetary burden of such a repayment of non-creditable foreign withholding taxes (excess credits). In line with Geelhoed's reasoning as to the source state's obligations, which the ECJ appears to have embraced, one could argue that the home state may satisfy its obligations under Community law by imposing the obligation on a source state, under a tax treaty, to either reimburse the home state for this refund (if the home state

pays the refund to the shareholder), or to pay out the refund of excess credits directly to the shareholder.

5.4. Extension of domestic exemption to non-resident shareholders

The Netherlands has opted for yet another alternative. Before the decision in the *Amurta* case was given it had already introduced, with effect from 1 January 2007, an exemption for dividend withholding tax paid to non-resident EU corporate shareholders in Art. 4 of the DWTA, comparable to that applicable to domestic parent companies. The withholding tax exemption for non-resident shareholders largely mirrors Art. 2 of the Parent-Subsidiary Directive, and, therefore, slightly differs from the exemption granted to resident corporate shareholders.⁵⁵ In addition, with effect from 2007, the existing refund mechanism for dividend withholding tax levied on tax (resident) exempt entities (for example Netherlands foundations and pension funds),⁵⁶ was extended to include entities that are resident in another Member State that are exempt from corporate income tax in that state and that would also have been exempt from Netherlands corporate income tax if they had been a tax resident of the Netherlands.⁵⁷

5.5. Dividend withholding tax: a discriminatory levy?

In his lecture on 14 December 2006, Geelhoed did not touch upon the fundamental question as to whether Member States are allowed to levy a dividend withholding tax at all. In the Netherlands, for instance, withholding tax levied from a resident shareholder, either a corporate shareholder or an individual, is in nearly all situations⁵⁸ creditable against the income tax of a resident shareholder, and cash refundable in the event of an excess credit. For domestic shareholders, therefore, dividend withholding tax is not a real tax burden, but a form

52. *Gilly*, note 19, Paras. 46-48.

53. *Id.*, Para. 49.

54. See *ACT Group Litigation*, note 17, Para. 60.

55. In principle, this new regime provides for a dividend withholding tax exemption if:

- the shareholder is a tax resident of another Member State;
- the non-resident shareholder owns 5% or more of the shares in the distributing company, or owns an interest that would otherwise qualify for the participation exemption if the shareholder would have been a tax resident of the Netherlands; and
- the non-resident shareholder and the distributing company have a legal form mentioned in the Annex to the Parent-Subsidiary Directive; if they are subject (without an option and without being exempted) in their Member State of residence, to one of the corporate income taxes mentioned in Art. 2 of the Parent-Subsidiary Directive; and if they are not a tax resident in a third country according to a tax treaty with such third country.

56. Art. 10 DWTA.

57. In particular this latter requirement will be difficult to satisfy for non-resident entities, because they have to meet the criteria for tax-exempt status both in their Member State of residence and in the Netherlands. It can be assumed that this double test results in non-resident entities being treated less favourably than Netherlands resident (exempt) entities. Finally, with the introduction of a special regime for exempt investment funds as per 1 August 2007, these investment funds are not entitled to a refund of Netherlands dividend withholding tax. This carve out from the refund mechanism has also been extended to tax-exempt investment funds resident in another Member State.

58. I.e. not if the dividends are paid to an exempt investment fund.

of advance payment with respect to their final income tax liability. This means that, in fact, almost the whole amount of dividend withholding tax – which is not credited by or refunded to domestic shareholders – is collected from non-resident shareholders, as was recently confirmed by the Netherlands state secretary of Finance De Jager⁵⁹ in Parliament. Due to this highly (indirect) discriminatory nature, the question arises as to whether dividend withholding tax, as such, is contrary to the freedoms of the EC Treaty. In discussing the abolishment of this tax (in another context), state secretary of Finance De Jager referred to the fact that this would primarily benefit the budgets of other states, because in most situations the Netherlands dividend withholding tax is creditable in the home states of the foreign shareholders in any event. In fact, he argued that such abolishment would only result in a shift of apportionment of taxing powers between the states, and that it is internationally accepted that a source state levies a withholding tax in addition to corporate income tax on the profits generated in its territory. However, the fact that the levy of dividend withholding tax (in addition to corporate income tax that is levied from the distributing company) by a source state is part of the internationally accepted tax practice, and has also been embedded in the OECD Model, does not necessarily mean that such a levy is not contrary to the EC Treaty.⁶⁰

6. Conclusions

Dividend withholding tax plays an important role in the taxation of cross-border dividend payments within the European Union that fall outside the scope of the Parent-Subsidiary Directive. Dividend withholding tax may cause both juridical and economic double taxation of dividends. It will be extremely difficult for the ECJ to find a fundamental solution to the distortions and disparities caused by this levy. For the time being, the ECJ can only remove discriminatory elements embedded in the national withholding tax regimes on a case-by-case basis. Gradually and carefully, however, the ECJ has begun to recognize, along the lines set forth by Geelhoed, the differences between home state and source state obligations when it comes to the prevention or mitigation of economic double taxation. Tax treaties between the source state and the home state have also started to play a relevant role when it comes to neutralizing a discriminatory withholding tax system of one Member State. The author has developed further thoughts along these lines on how Member States could comply with Community law in respect of the taxation of cross-border dividend flows.

59. EK 2007-2008, 31.205/206, No. C (*nota naar aanleiding van het verslag*), pp. 38-39. In 2005 more than 90% of the net dividend withholding tax collected was collected from non-resident shareholders (see O.C.R. Marres and P.J. Wattel, *Dividendbelasting* (Fiscale studiereserie, No. 26), 3rd edition (Deventer: Kluwer, 2006), p. 4.).

60. See *Bouanich*, note 17, Para. 50.