

THE ABERDEEN CASE: WITHHOLDING TAX ON DIVIDENDS DISTRIBUTED BY A FINNISH COMPANY TO A LUXEMBOURG SICAV IS DISCRIMINATORY

This judgement gives possibilities to investment funds to claim a refund of withholding taxes unduly paid in the Member States where they made investments.

A/ FACTS AND BACKGROUNDS

The present case concerns a Finnish resident real estate company, Aberdeen Property Fininvest Alpha Oy ("Alpha"), held 100% by an open-ended investment company established and governed by the law of Luxembourg, Aberdeen Property Nordic Fund I SICAV ("Nordic Fund SICAV").

In the case at hand, Alpha asked the Keskusverolautakunta (the Finnish tax administration), whether dividends distributed to its parent company, a Luxembourg SICAV, could be exempted from Finnish withholding tax. The argument in favour of such exemption was mainly based on the discriminatory nature of such taxation with respect to EU law.

Further to the refusal of the Finnish tax administration, Alpha submitted the issue to Finnish courts which decided to refer the matter to the European Court of Justice ("ECJ").

The ECJ had to decide whether it was contrary to article 43 (freedom of establishment) and article 56 (free movement of capital) of the EC Treaty to charge Finnish withholding tax on dividends distributed by a Finnish company to a non-resident company incorporated as a Luxembourg SICAV when such dividends distributed to a resident Finnish share capital company or investment fund would have been exempted.

B/ ECJ DECISION

First of all, the ECJ examined the problem regarding the Parent-Subsidiary Directive (the “Directive”) and ruled that a Luxembourg SICAV does not enter into the scope of the Directive. The ECJ also specified, in respect of shareholdings which are not covered by such Directive that, Member States have to establish, individually or conventionally with other Member States, procedures in order to avoid or mitigate double taxation. As a matter of course, the ECJ also specified that these measures should comply with the freedoms guaranteed by the EC Treaty.

The ECJ then investigated whether the difference in tax treatment of the dividends could create a restriction to the principle of freedom of establishment. On this point, the ECJ ruled that such a difference of treatment of dividends, when based on the place of residence of the parent company constitutes a restriction to the freedom of establishment prohibited by articles 43 and 48 of the EC Treaty. Indeed, these articles prevent a company from acquiring, creating or maintaining a subsidiary in the Member State applying such difference in tax treatment. Consequently, referring to the Denavit case, the ECJ stated that a Member State which decides to protect resident parent companies by eliminating double taxation of the dividends received by a resident parent company, should apply the same rule to non-resident parent companies in a comparable situation.

The ECJ rejected all the arguments of the Finnish and Italian Governments (which had commented on the matter) to justify this restriction of freedom.

Indeed, the ECJ held that:

1. As the Finnish tax regime does not aim at preventing artificial arrangements, the Finnish rules cannot be justified by the fact that the Finnish government wish to prevent tax avoidance.
2. As Finland does not apply withholding tax on dividends received by Finnish companies, it cannot argue that there is a need to ensure the balanced allocation of the power to tax between Member State in order to justify withholding on dividends received by companies established in another EU Member State;
3. At last, in the case at hand, there is no link between the exemption of the withholding tax and the offsetting of that tax advantage by a particular tax levy which could justify a restriction needed to preserve the coherence of the Member State’s tax system.

The ECJ concluded that the Finnish legislation was discriminatory and contrary to EU freedoms.