

# Legislation

## Austria, United Kingdom

### AUSTRIA

#### CHANGES TO AUSTRIA'S TAX TREATMENT OF INBOUND INTER-COMPANY DIVIDENDS

As reported in previous issues of the *EC Tax Review*,<sup>1</sup> Austria's treatment of inbound inter-company dividends has been heavily discussed in the light of the EC fundamental freedoms. This is because dividends received by a company resident in Austria from domestic companies are always tax-exempt, while, in contrast, dividends from foreign companies were only exempt if a minimum holding requirement (10%) and a holding period (one year) were fulfilled (so-called international participation exemption). The Austrian Supreme Administrative Court (VwGH) found that in intra-EU situations, such treatment is in violation of the free movement of capital under Article 56 EC,<sup>2</sup> but that such discrimination may be cured by granting an indirect foreign tax credit for the underlying corporate tax instead of an exemption.<sup>3</sup> This position was also adopted by the Austrian Federal Ministry of Finance,<sup>4</sup> but the foundations and the details of this solution were subsequently referred to the European Court of Justice (ECJ) by the Tax Senate (UFS) of Linz in C-436/08, *Haribo*, and C-437/08, *Österreichische Salinen*.<sup>5</sup>

Without awaiting the ECJ's ruling in these cases, the Austrian legislator has recently reacted to this development in the Budget Supplementary Act 2009.<sup>6</sup> While the 'old' regime of the 'international participation exemption' and the respective antiabuse provision<sup>7</sup> remain substantially unchanged, new rules were introduced in section 10(1)(4) and (5) of the Corporate Tax Act to also cover 'portfolio dividends'.<sup>8</sup> These rules provide for a straightforward exemption for all dividends<sup>9</sup> from EU companies and from qualified European Economic Area (EEA) companies (i.e., with comprehensive exchange of information and recovery of tax claims, which is currently only the case with Norway).<sup>10</sup> The legislation, however, also introduced a new antiabuse rule in section 10(5); otherwise, qualifying portfolio dividends are not exempt from tax if the foreign distributing company is subject to 'low taxation', irrespective of whether or not the distributing company derives active or passive income. 'Low taxation' is assumed if (1) the distributing company is not effectively being

subject to a corporate income tax comparable to the Austrian corporate income tax or (2) the nominal foreign corporate income tax applicable is lower than 15% or (3) the foreign distributing company enjoys

<sup>1</sup> See Georg Kofler, 'Austria: Supreme Administrative Court rules on EC-Compatibility of the International Participation Exemption Regime', *EC Tax Review* 6 (2008): 293, and Georg Kofler, 'Austria: Requests for Preliminary Rulings Concerning the EC-Incompatibility of Austria's International Participation Exemption Regime: C-436/08, *Haribo*, and C-437/08, *Österreichische Salinen*', *EC Tax Review* 1 (2009): 57.

<sup>2</sup> See VwGH, 17 Apr. 2008, 2008/15/0064, available at [www.ris.bka.gv.at/vwghz](http://www.ris.bka.gv.at/vwghz); the preceding decision was by the UFS Linz, 13 Jan. 2005, RV/0279-L/04, available at <https://findok.bmf.gv.at>.

<sup>3</sup> For a discussion see Thomas Bieber, Werner Haslehner, Georg Kofler et al., 'Taxation of Cross-Border Portfolio Dividends in Austria: The Austrian Supreme Administrative Court Interprets EC Law', *European Taxation* 11 (2008): 583–589, with further references.

<sup>4</sup> This information (BMF-010216/0090-VI/6/2008) was published on 13 Jun. 2008; it is available (in German) at <https://findok.bmf.gv.at>, and was reprinted in *Finanz Journal* (2008): 274, in *Österreichische Steuerzeitung* (2008): 270, and in *Steuer- und Wirtschaftskartei* (2008): S 528 et seq.

<sup>5</sup> For a brief discussion of these references, see Georg Kofler & Clemens Ph. Schindler, 'Haribo. Request for a Preliminary Ruling in Austrian Case on Foreign Participation', *H&I* (2009): 59–69.

<sup>6</sup> *Federal Gazette* (BGBl) I 2009, nr. 52; for a discussion of the draft legislation, see Georg Kofler & Clemens Ph. Schindler, 'Finance Ministry Targets Participation Exemption Regime', *Tax Notes Int'l* 53 (30 Mar. 2009): 1163–1165.

<sup>7</sup> This provision is designed to prevent resident companies from benefiting from the international participation exemption if the focus of the nonresident subsidiary's business operations consists directly or indirectly in deriving interest income, income from the leasing of assets, or the sale of participations ('passive income') and has been subject to low taxation, i.e., a foreign tax burden of less than 15%. In such case s. 10(4), (6) foresees a switch-over to the indirect credit method.

<sup>8</sup> That is, dividends derived from shareholdings below the 10% threshold of the 'international participation exemption regime', irrespective of how long the shares are being held.

<sup>9</sup> The exemption for capital gains from the alienation of shares in a foreign company is only available under the 'international participation exemption regime', which has a minimum holding requirement (10%) and a minimum holding period (one year); however, and unlike the new exemption for EU- and EEA-portfolio dividends, the 'international participation exemption regime' also applies to third-country subsidiaries and all EEA subsidiaries irrespective of information exchange or assistance in the recovery of tax claims.

<sup>10</sup> For portfolio dividends from third countries, the treatment remains unchanged, i.e., they are subject to corporate income tax at the rate of 25%.

far-reaching exemptions from tax (unless they are comparable to Austria's exemptions for dividends and capital gains). In these cases, the dividends are not exempt from taxation, but rather an indirect foreign tax credit for the underlying corporate tax will be granted under section 10(5).

The new rules apply retroactively to all open<sup>11</sup> cases and hence are an elegant way to do away with many of the previously existing discriminations. Nevertheless, some issues remain doubtful in the light of EC law. First, the straight-out exclusion of third-country companies and non-qualified EEA companies (i.e., Iceland and Liechtenstein companies) raises questions as to the compatibility with Article 56 EC and the EEA Agreement.<sup>12</sup> Second, in the case of a switch-over to the credit method (based on foreign 'low taxation'), it may be doubted whether the indirect credit method is indeed equivalent to exemption, especially when it comes to the amount of creditable tax and the question of a credit carry-forward in loss situations.<sup>13</sup> Third, in a switch-over situation, the domestic minority shareholder might not even be able to meet the burden of proof (e.g., concerning the amount of foreign corporate tax levied, especially when dividends are received through an investment fund), which raises the question whether it is for the tax administration to make use of the Mutual Assistance Directive<sup>14</sup> to gather such information.<sup>15</sup> It is hoped that the ECJ will provide some clarification of these issues in *Haribo* and *Österreichische Salinen*.

<sup>11</sup> Section 26c(16)(b) CITA.

<sup>12</sup> See, e.g., Ernst Marschner & Markus Stefaner, 'Die Zulässigkeit von Einschränkungen der Kapitalverkehrsfreiheit gegenüber Drittstaaten aufgrund fehlender Amts- und Vollstreckungshilfe', *Steuer und Wirtschaft International* (2009): 372, 383–384.

<sup>13</sup> See for this discussion, e.g., Christian Massoner & Birgit Stürzlinger, 'Anrechnungsmethode als geringster und gemeinschaftsrechtskonformer Eingriff in die Besteuerung von Portfoliodividenden', *Steuer und Wirtschaft International* (2008): 400, 407; Christian Massoner & Birgit Stürzlinger, 'Gleichartigkeit von Anrechnungs- und Befreiungsmethode aus gemeinschaftsrechtlicher Sicht: (An-)Rechnung ohne Wirt?', *Steuer und Wirtschaft International* (2009): 280, 280 et seq.; see also the reasoning of the UK High Court in the judgment of 27 Nov. 2008 in *FII Group Litigation* [2008] EWHC 2893 (Ch).

<sup>14</sup> Council Directive of 19 Dec. 1977 concerning mutual assistance by the competent authorities of the Member States in the field of direct taxation and taxation of insurance premiums (77/799/EEC) [1977] OJ (L336), 15, as amended.

<sup>15</sup> See, e.g., Gernot Aigner & Babette Prechtl, 'Ermittlung der anrechenbaren ausländischen Körperschaftsteuer bei Portfoliodividenden!', *Steuer- und Wirtschaftskartei* (2008): S 761 et seq., and Babette Prechtl, 'Steuerpflicht von Portfoliodividenden erneut auf dem Prüfstand', *Steuer und Wirtschaft International* (2008): 497, 498 et seq.

tax exemption for dividends to qualified EU parent companies for shareholdings of at least 10%.<sup>1</sup> Below this threshold, outbound dividends are in principle subject to a final withholding tax of 25% or the lower treaty rate, respectively. Such withholding tax is also applied to portfolio dividends in domestic settings, but credited or refunded to the domestic corporate recipient, as inter-company dividends are effectively exempt under Austria's domestic participation exemption regime. Such refund was, however, not available to foreign corporate shareholders. This obvious difference in treatment has not only been criticized in legal writing from the perspective of the freedom of capital movement,<sup>2</sup> but has also resulted in the initiation of an infringement proceeding by the Commission.<sup>3</sup> The European Court of Justice's (ECJ's) recent case law<sup>4</sup> on the taxation of outbound dividends has intensified the doubts as to the compatibility of Austria's regime with EC law. According to this line of case law, however, a difference in treatment is permissible if the dividend receiving company can claim a tax treaty credit for the source country's withholding tax, as in such case the discrimination may be 'neutralized'.<sup>5</sup>

In the Budget Supplementary Act 2009,<sup>6</sup> the Austrian legislator has reacted to these developments by introducing a refund mechanism for foreign corporate shareholders in section 21(1)(1a) of the Corporate Tax Act. Without regard to a minimum holding requirement or a holding period, EU companies and qualified European Economic Areas (EEA) companies (i.e., with comprehensive exchange of information and recovery of tax claims, which is currently the case only with Norway) may claim a repayment of dividend withholding tax insofar as such withholding tax cannot be credited in their respective residence States under a tax treaty.<sup>7</sup> The foreign dividend receiving company has to provide

<sup>1</sup> Section 94(a) of the Income Tax Act.

<sup>2</sup> See, e.g., Ernst Biebl, 'EuGH-Entscheidung Denkavit und ihre Folgen für die österreichische Quellenbesteuerung', *Steuer & Wirtschaft International* (2007), 65, 72; Georg Kofler & Michael Tumpel, 'Amurta: Diskriminierende Quellenbesteuerung und Anrechnungsmethode', *Österreichische Steuer-Zeitung* (2008), 54, 58–59.

<sup>3</sup> See the Commission's Press Release IP/07/1152.

<sup>4</sup> ECJ, 14 Dec. 2006, C-170/05, *Denkavit Internationaal BV and Denkavit France SARL v. Ministre de l'Économie, des Finances et de l'Industrie*, [2006] ECR I-11949 and ECJ, 8 Nov. 2007, C-379/05, *Amurta v. Inspecteur van de Belastingdienst*, [2007] ECR I-9569 (hereinafter 'Amurta').

<sup>5</sup> Amurta, para. 79; see also ECJ, 12 Dec. 2006, C-374/04, *Test Claimants in Class IV of the ACT Group Litigation v. Commissioners of Inland Revenue*, [2006] ECR I-11673, para. 71. For an even broader approach, see Eric Kemmeren, 'ECJ Should Not Unbundle Integrated Tax Systems!', *EC Tax Review* 17 (2008): 4, 9, and *id.*, 'The Internal Market Approach Should Prevail over the Single Country Approach', in *A Vision of Taxes within and outside European Borders – Festschrift in honor of Frans Vanistendael*, eds L. Hinnekens & Ph. Hinnekens (Alphen aan den Rijn: Kluwer, 2008), 555, 561–564 (arguing to consider also unilateral relief).

<sup>6</sup> Federal Gazette (BGBI) I 2009, nr. 52.

<sup>7</sup> According to s. 21(1)(1a) of the Corporate Tax Act such (partial) refund has to be claimed with the tax office that is responsible for assessment of the Austrian distributing company.

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As required by the Parent-Subsidiary Directive, Austrian law generally provides for a withholding

proof that the Austrian withholding tax cannot (fully or partly) be credited in its residence State, for example, by providing an assessment notice; in practice, such proof of non-creditability will be easy to provide if the foreign country employs a participation regime, but difficulties will arise if a credit carry-forward is available.

Section 21(1)(1a) of the Corporate Tax Act entered into force on 18 June 2009 and thus does not deal with withholding taxes that were levied before that date in violation of the EC Treaty's fundamental freedoms. In these cases, a refund of such withholding taxes may arguably be claimed under general principles in the light of the ECJ's jurisprudence (unless a tax treaty credit was available in the shareholder's residence State).<sup>8</sup> Furthermore, the new rule does not address dividend withholding taxes on distributions to non-qualified EEA companies (i.e., without comprehensive exchange of information and recovery of tax claims) and companies in third countries: As for the EEA, the Ministry of Finance excludes refunds to companies resident in Iceland and Liechtenstein based on the consideration that those countries do not provide exchange of information and assistance in the recovery of tax claims.<sup>9</sup> However, while it seems permissible to require exchange of information,<sup>10</sup> it is not entirely clear whether assistance in the recovery of tax claims is in fact necessary and may as such provide a justified requirement. As for third countries, it seems questionable whether a straight-out exclusion without regard to tax treaty provisions on exchange of information can be upheld in the light of Article 56 EC,<sup>11</sup> the application of which to portfolio investments (below 10%) by third country companies is arguably neither excluded by the freedom of establishment nor by the grandfather clause of Article 57 EC.<sup>12</sup>

*Georg Kofler  
Johannes Kepler University Linz*

<sup>8</sup> See, e.g., Katharina Haslinger, 'Die Besteuerung von Dividenden – EuGH bestätigt Kritik an geltender Rechtslage', *Steuer & Wirtschaft International* (2007), 175, 180; and Kofler & Tumpel, *supra* n. 2. Such refund claims have to be addressed to the tax office Bruck-Eisenstadt-Oberwart, which has a special competence for refunds based on international agreements; see the Ministry's information in EAS 3012, available (in German) at <<https://findok.bmf.gv.at>>, and reprinted in *Steuer & Wirtschaft International* (2009), 8.

<sup>9</sup> See EAS 2956, reprinted in *Steuer & Wirtschaft International* (2008), 204, and EAS 2976, reprinted in *Steuer & Wirtschaft International* (2008), 286; both are available (in German) at <<https://findok.bmf.gv.at>>.

<sup>10</sup> ECJ, 11 Jun. 2009, C-521/07, *Commission v. The Netherlands*, *nyr*, paras 47 and 48.

<sup>11</sup> See, e.g., ECJ, 18 Dec. 2007, C-101/05, *Skatteverket v. A*, [2008] ECR I-11531 (hereinafter 'A'), paras 54 et seq.

<sup>12</sup> A, para. 21; ECJ, 20 May 2008, C-194/06, *Staatssecretaris van Financiën v. Orange European Smallcap Fund NV*, [2008] ECR I-3747, paras 87 and 88.