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Government Considering Expansion Of Dividend Exemption

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COUNTRY DIGEST

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Government Considering Expansion Of Dividend Exemption

Just over a month after the European Court of Justice issued its judgment in the joined cases *Haribo* (C-436/08) and *Salinen* (C-437/08), Austria's Ministry of Finance has published draft legislation proposing a two-step process to expand the tax exemption for foreign dividends received by an Austrian corporation. (For the ECJ's February 10 judgment, see *Doc 2011-2905* or *2011 WTD 29-18*.)

Austria previously had addressed the issue of double taxation of dividend income by adopting a system under which dividends paid between corporations in a purely domestic context were tax-exempt, as were dividends paid by foreign corporations to Austrian corporate shareholders that held a stake of at least 10 percent in the foreign corporation. Dividends paid by a corporation to individuals were taxed at a lower rate (25 percent) compared to the generally applicable progressive income tax rate.

The question that arose in *Haribo* and *Salinen* was whether Austria's dividend exemption for dividends at the purely domestic level should also apply to dividends received from the EU and the European Economic Area, as well as to dividends received from third countries, such as the United States.

When the preliminary ruling request on the issue was submitted to the ECJ by an Austrian Independent Fiscal Senate — which questioned a higher court's decision (for prior coverage, see *Doc 2009-2775* or *2009 WTD 47-8*) — the Austrian Legislature reacted by passing a legislative amendment to exempt dividends from EU and EEA member states. For dividends from EEA member states, however, the exemption applied only if an administration assistance and enforcement agreement was in place. (For prior coverage, see *Doc 2009-15169* or *2009 WTD 141-12*.)

In its final judgment in the joined cases, the ECJ's main findings were as follows:

- Dividends received by Austrian corporations from third countries are entitled to the tax benefit if it applies to domestic dividends.
- The benefit does not necessarily have to be a tax exemption. A credit for the tax paid by the dividend distributing corporation upon generating the distributable profit is also sufficient.
- The carryforward of any excess credit must be allowed.
- The question of whether withholding taxes on dividends of the source state are taken into account in the resident state is, in the case of *Haribo* and *Salinen*, a question of the involved countries' income tax treaties, and not a question of the EU principle of free movement of capital.
- Requiring an enforcement agreement in order to provide a tax benefit for dividends from EEA member states is not proportionate to the aim of the rule and therefore cannot be a condition for granting the tax benefit.

The new legislative proposal drafted by the Finance Ministry covers all those points: It extends the existing exemption for dividends received from corporations resident in EU and EEA member states to dividends received from any foreign corporation; provided that an agreement for comprehensive assistance in tax matters is in place with the resident country, no enforcement agreement is required.[1]

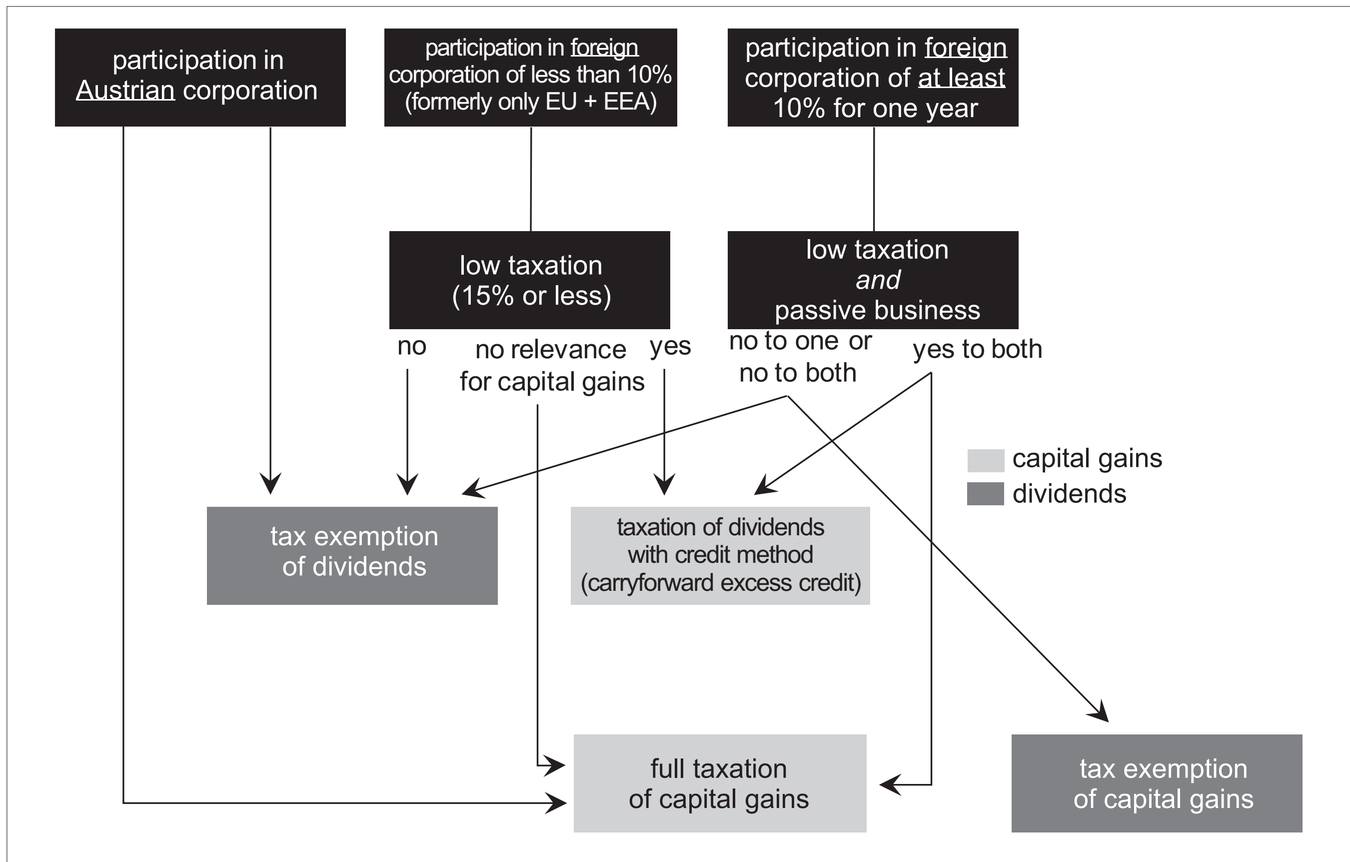
Furthermore, under current law, a switch from the exemption to the credit method is triggered in situations in which low taxation (15 percent or less) is imposed in the country of the distributing corporation. The proposed amendment provides for a carryforward of any excess credit resulting from such a switch.[2]

The figure illustrates, in a simplistic manner, how the new dividend tax regime for Austrian corporate shareholders will work if the Finance Ministry's proposal is implemented.

It should be noted that the impact of the ECJ judgment in *Haribo* and *Salinen* is not limited to the future.

[1] Proposed section 10(1)(6), Corporate Income Tax Act.

[2] Proposed section 10(6), last two sentences, CITA.



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Austrian corporate shareholders that paid tax on portfolio dividends before the judgment was issued can request either a refund of the tax or a dividend tax credit for the foreign taxes paid by the dividend distributing company. This is possible, at the least, for tax periods that have not been through a final assessment, because ECJ judgments do not change the law as of the date the judgments are issued; rather, they nullify national law that is in violation of EU law, thereby setting the national law aside from the date it was first put into place.[3] ◆

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[3]Craig and de Búrca, *EU Law*, p. 543; Michael Tanzer, ''Die Rückforderung gemeinschaftsrechtswidrig erhobener Abgaben,'' in: Holoubek and Lang (eds.), *Das EuGH-Verfahren ins Steuersachen*, p. 209.

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