Netherlands; Belgium

Advocate General Recommends Supreme Court Seek ECJ Ruling on Cross-Border Tax Set-Off Order

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In an opinion released on 15 December 2023, Advocate General (AG) Koopman suggested that the Supreme Court seek clarification on the sequence for offsetting tax credits and withholding taxes in cross-border scenarios.

(a) Facts. The case involves a Dutch resident taxpayer with minimal income tax liability in 2018. Despite the low-income tax owed, the taxpayer faced a significant payment of Belgian withholding tax on dividends during the same year. The withheld Belgian withholding tax is eligible for offset against the Dutch income tax per article 23 of the Belgium - Netherlands Income and Capital Tax Treaty (2001). This set-off, however, differs from the one applicable to Dutch dividend withholding tax. In domestic situations, the tax credits are first deducted from the tax, and then the dividend withholding tax is credited. However, foreign withholding taxes are deducted from the tax before the tax credits are deducted.

This difference is detrimental to the taxpayer because tax credits cannot be "carried over" to the next tax year, unlike offset withholding tax. Dutch dividend withholding tax is refunded immediately if insufficient tax is due, but foreign withholding tax is carried forward. Subsequently, the tax inspector issues a decision in the assessment, specifying the amount of foreign withholding tax to be offset in future years.

The taxpayer appealed the decision and cited the free movement of capital under article 63 of the Treaty on the Functioning of the European Union (TFEU). Additionally, in the appeal to the cassation court, the taxpayer invoked article 14 of the European Convention on Human Rights (ECHR), prohibiting discrimination, and article 1 of the First Protocol to the ECHR, safeguarding the right to peaceful enjoyment of property.

(b) Legal background. Article 2.7 of the Income Tax Act (ITA) describes the order of the offset of the tax credits and withholding tax. Article 9.2. of the ITA provides for a credit of dividend withholding tax against income tax.

(c) Issue. The central issue revolved around the compatibility of the disparate treatment of domestic and foreign withholding tax with the principles of the free movement of establishment and/or free movement of capital as outlined in the Treaty on the Functioning of the European Union (TFEU).

(d) Opinion. The Arnhem-Leeuwarden Court of Appeal on 23 February 2023 concluded that the circumstances of a domestic taxpayer receiving dividends with withheld dividend tax are not objectively comparable to those of a taxpayer receiving dividends from a Belgian company with Belgian withholding tax. According to the Court of Appeal, article 2.7 of the ITA 2001 is, therefore, compatible with the free movement of capital of the TFEU.

The AG overturned that decision, determining that the taxpayer is not entitled to seek a refund of the Belgian withholding tax in their 2018 assessment as if it were Dutch dividend withholding tax. EU law does not require Member States to refund withholding taxes levied by other Member States. The AG had expressed uncertainty regarding whether the sequence in which tax credits and foreign withholding taxes are offset can deviate from the order in which tax credits and Dutch dividend withholding tax are offset. This position stems from an ECJ decision in Imfeld and Garcet (Case C-303/12) which declared that legislation of a Member State that denies a tax advantage to residents earning income from two Member States, while granting that advantage to residents earning income only from sources in that Member State, is incompatible with the freedom of establishment.

The AG reasoned that if the taxpayer was correct in his assertion that the different order of set-off in cross-border situations constituted an obstacle to the free movement of capital, then this difference was not justifiable. It could not be justified by overriding reasons related to the general interest, it might not have been suitable for achieving the objective pursued, and it could have gone beyond what was necessary to achieve that objective.

Furthermore, the AG concluded that the reliance on article 14 of the ECHR and article 1 of the FP to the ECHR is not beneficial for the taxpayer. This is because those provisions do not possess an independent significance beyond the reliance on the freedoms outlined in the EU treaty.

Consequently, the AG proposes that the Supreme Court should request a preliminary ruling from the ECJ.

The AG opines to request a preliminary ruling on the following question:

Is article 49 of the TFEU to be interpreted as precluding the application of tax legislation of a Member State, such as that at issue in the main proceedings, which has the effect of depriving residents of that State of a certain tax advantage (tax credits) in relatively rare cases as a result of the fact that the income tax which they are liable to pay is first reduced by withholding tax on dividends withheld by another Member State? whereas those residents would receive the tax credits if the withholding tax had been withheld by the Member State in which they reside, and is it relevant in that regard whether the tax payable in that State is already nil before the tax credits have been deducted?
