

6 JULY 2009

PRESS STATEMENT



TAX DISCRIMINATION OF FOREIGN PENSION FUNDS

EUROPEAN COMMISSION AND COURTS' DECISIONS ARE PRODUCING TANGIBLE RESULTS

EFRP is happy to note progress and considers it is an appropriate moment to provide an overview of recent and significant developments regarding the discriminatory taxation of foreign EU based pension funds. Working further on the complaints lodged by EFRP in December 2005, the Commission has initiated a number of infringement proceedings which are bearing fruits already since national courts are following the Commission's reasoning that Member States' rules on withholding tax on dividends and interest do not respect the principle of free movement of capital in the European Union.

The most recent move is the Commission decision of 25 June 2009, to send **Denmark** and **Finland** formal requests to change their legislation to end the discriminatory taxation against foreign pension funds. The Commission's requests take the form of a 'reasoned opinion' (second step of the EU infringement procedure of Art. 226 EC Treaty). In Finland, dividends paid by a company which is resident in Finland to a non-resident pension fund, are subject to a withholding tax on gross income at a rate of 19,5% while tax on dividends paid to Finnish pension funds is 19,5% on the net income, i.e. after deduction of costs and current pension liabilities. In practice, then, the effective tax rate on dividend income paid to a Finnish pension fund will be lower than the tax rate on dividends paid to foreign pension funds as the latter cannot benefit from a reduction of the tax base on which the withholding tax is applied. The same goes in Denmark where dividends paid to foreign pension funds are effectively subject to a tax rate of 15% on the gross amount of the dividend,

whereas Danish domestic pension funds are subject to a yield tax of 15% on a net basis.

Earlier, the 14 May 2009, the Commission had already sent a reasoned opinion to **Poland** requesting that Member State to end its discriminatory taxation of non-resident pension funds. Polish pension funds are exempt from corporate income tax, and thus dividends and interest received by domestic pension funds are tax exempt. However, Poland levies a withholding tax of 19% on dividends paid to foreign pension funds and a withholding tax of 20% on interest paid to such funds unless a double tax treaty applies. According to the Commission, this infringes the free movement of capital and the freedom of establishment as provided for in Articles 56 and 43 of the EC Treaty. In addition, where non-resident financial institutions in Poland are obliged to pay a withholding tax on the gross amount of the interest received, domestic financial institutions are taxed on their net profits only. The Commission opines that this restricts the right of foreign financial institutions to deduct related costs and infringes Article 49 EC (freedom to provide services) and Article 56 EC. Poland has two months to react to the Commission which, if unsatisfied with the Polish reply, may refer the case to the European Court of Justice.

In recent months the **Dutch and Austrian** tax authorities have unilaterally started reimbursing dividend withholding tax claims by non-resident (EU and EEA based) pension funds. The Dutch tax authorities have said that the decision was triggered by ECJ case law developments and decisions of the Dutch Supreme Court supporting them. This trend is very good news for the European pension industry and it is to be expected that more countries will follow suit over time.

On 30 April 2009, the **Spanish Ministry of the Economy and Finance** issued a press release saying it is preparing amendments to the Spanish non-residents income tax act in order to end the discriminatory treatment of non-resident EU

based pension funds and that dividends and gains paid to non-resident pension funds will be exempt from taxation. The government's announcement indicates an awareness that the Spanish legislation may be in breach of EU rules. This is a welcome new development as the Commission announced on 27 November 2008 that it had referred Spain (and also Portugal), to the European Court of Justice for its refusal to amend the legislation in line with the EC Treaty.

On 13 February 2009, the **French Supreme Court** ('Conseil d'Etat') decided that the tax treatment of French dividends received by French pension funds under domestic tax law should be extended to EU non-profit organisations of the same nature. Four Dutch pension funds had asked for the annulment of the French Statements of Practice issued in 2005 which deny a withholding tax exemption on French source dividends to non-resident pension funds. This decision provides crucial arguments for further litigation in France and may open new opportunities for refund claims in France. The French Government will now need to take a formal position on this. In parallel, the Commission is preparing a Reasoned Opinion against France by which it will formally ask it to change its legislation.

In addition, as from 1 January 2009, the **Czech Republic and Estonia** have amended their corporate income tax acts which have ended the discrimination.

From the above it transpires that an increasing number of the originally identified 18 EU Member States have either already aligned their legislation with the EC Treaty or have promised to do so, while others are still negotiating with the Commission including Denmark, Finland, Germany, and Sweden. The Commission may decide to refer Italy to the ECJ, as it has already done with Portugal and Spain.

Background – Note to editors

The European Federation for Retirement Provision (EFRP) lodged complaints with the EU Commission in December 2005 against 18 EU member states aimed at ending their discrimination against non-resident EU based pension funds concerning the taxation of dividends and interest. The Commission agreed that this practice breaches EU rules on the free movement of capital (Article 56 EC Treaty).

Based on the complaints, in May 2007, the Commission started EU infringement proceedings against these Member States. In parallel, a number of recent court judgments at both EU and national level have confirmed and reinforced the view of the Commission. In December 2006 for instance, the European Court of Justice established that in the European Union, outbound dividends cannot be subject to higher taxation in the source State than domestic dividends. The combined pressure of the Commission's action and ECJ and national court decisions is now starting to produce concrete results.

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About the EFRP

The European Federation for Retirement Provision represents the various national associations of pension funds and similar institutions for pension provision. The EFRP has members in most EU Member States¹.

To address the concerns of Central and Eastern European Countries – CEEC - it has established in October 2006 the CEEC Forum. Membership of this Forum is open to representatives of private pension institutions from EU-12 Member States that over the recent years have made multi-pillar pension reform.

EFRP membership at large consists of institutions for occupational (2nd pillar) retirement some of them also operating purely individual pension schemes (3rd pillar).

Most EFRP members in EU-15 are non-profit making associations. Members and beneficiaries are usually represented in their governance structures; many of them are managed on a paritarian basis between unions/employees and employers.

73 million EU citizens are covered for their occupational pension plan by EFRP Member Associations.

Through its Member Associations the EFRP represents € approximately 3 trillion of assets (2007) managed for future occupational pension payments.

¹ EFRP has members in: Austria, Belgium, Finland, France, Germany, Hungary, Ireland, Italy, Netherlands, Portugal, Romania, Slovakia, Spain, Sweden, the UK, and also in non-EU Member States: Croatia, Guernsey, Iceland, Norway and Switzerland.