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Press and Information

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Judgment of the Court of Justice in Case C-170/05

*Denkavit Internationaal BV, Denkavit France SARL v Ministre de l'Économie, des Finances
et de l'Industrie*

**NATIONAL LEGISLATION WHICH MAKES DIVIDENDS RECEIVED BY A NON-
RESIDENT PARENT COMPANY LIABLE TO A WITHHOLDING TAX, WHILE
ALMOST FULLY EXEMPTING DIVIDENDS RECEIVED BY A RESIDENT
PARENT COMPANY, RESTRICTS FREEDOM OF ESTABLISHMENT**

*Freedom of establishment precludes such a withholding tax, even if a tax convention
authorises the non-resident parent company to offset it against the tax due in the State in
which it is resident, where that parent company is unable to offset that tax*

Under French law, as in force at the relevant time, dividends paid by a French-resident company to a parent company which was not resident in France gave rise to a withholding tax at the rate of 25%. In the case of dividends paid by a French-resident company to a parent company which was also resident in France, no withholding tax was levied. Furthermore, a parent company having its seat or a permanent place of business in France was entitled, subject to certain conditions, to an almost full exemption from tax in respect of dividends paid by its subsidiary. Apart from a 5% share, such dividends did not form part of the net taxable profits of the parent company and were accordingly exempt from tax.

In addition, a Franco-Netherlands Convention¹ for the avoidance of double taxation provided that a Netherlands-resident parent company was entitled to offset the tax levied in France against the amount of tax payable in the Netherlands. The amount offset could not exceed the amount of the Netherlands tax due in respect of those dividends. Since Netherlands

¹ Convention between the Government of the French Republic and the Government of the Netherlands for the Avoidance of Double Taxation and the Prevention of Tax Evasion in respect of Taxes on Income and Wealth, signed at Paris on 16 March 1973.

companies were exempt in that country from tax on foreign-sourced dividends, it followed that no credit was available as regards the French withholding tax.

Denavit Internationaal BV is a parent company, resident in the Netherlands, which had at the relevant time two French subsidiaries, Agro-Finances SARL (which subsequently merged with Denavit France) and Denavit France, almost all of the capital of which was under its control. From 1987 to 1989, those two companies paid FRF 14.5 million by way of dividends to their parent company, Denavit Internationaal. In accordance with the Franco-Netherlands Convention and the French legislation, a withholding tax of 5% of the amount of those dividends was levied, corresponding to FRF 725 000.

Denavit Internationaal and Denavit France claimed repayment of that sum before the Conseil d'État, which has asked the Court to rule on the compatibility of the French withholding tax system with Community law.

The Court of Justice notes first of all that, although direct taxation falls within the competence of the Member States, they must none the less exercise that competence in a manner consistent with Community law.

Next, it states that freedom of establishment grants to Community nationals the right for companies formed in accordance with the law of a Member State to exercise their activity in the Member State concerned through, inter alia, a subsidiary. **Freedom of establishment thus seeks to guarantee the benefit of national treatment in the host Member State of the subsidiary, by prohibiting any discrimination, even minimal, based on the place in which companies have their seat.**

Such discrimination consists in applying a difference in treatment where there is no objective difference between situations such as to justify that difference in treatment.

The Court holds that, irrespective of the Franco-Netherlands Convention, the national legislation gives rise to a difference in the tax treatment of dividends paid by a resident subsidiary to its parent company, according to whether the latter is resident or non-resident.

Thus, while resident parent companies may be entitled to almost full exemption from tax on dividends received, non-resident parent companies are, by contrast, subject to tax in the form of a withholding tax of 25% of the amount of dividends paid.

In addition, unlike dividends paid to resident parent companies, those paid to non-resident parent companies are subject to a series of charges to tax under French tax legislation. Thus, those dividends are subject to tax, first, in the form of corporation tax levied on the resident subsidiary making the distribution and, second, in the form of the withholding tax levied on the non-resident parent company receiving the dividends.

Accordingly, **such a difference in the tax treatment of dividends paid to parent companies, based on the place in which they have their seat, constitutes a discriminatory restriction on freedom of establishment.**

With regard to the Franco-Netherlands Convention, the Court notes that, in the absence of harmonisation at Community level, the Member States, so long as they act consistently with Community law, retain competence for determining the criteria for taxation on income and may, if appropriate through conventions, prevent double taxation and determine the connecting factors in order to allocate fiscal jurisdiction between the Member States.

Reaffirming the principle that **a restriction on the freedom of establishment is prohibited, even if it is of limited scope or minor importance**, the Court holds that it follows from the combined application of the Franco-Netherlands Convention and the Netherlands legislation that resident parent companies benefit from a tax regime which allows them to avoid the imposition of a series of charges to tax and that non-resident parent companies are, by contrast, subject to such a form of taxation on dividends paid by their subsidiaries established in France.

Accordingly, **the Court holds that Community law precludes national legislation which imposes, only as regards non-resident parent companies, a withholding tax on dividends paid by resident subsidiaries, even if a tax convention between France and the Netherlands authorises that withholding tax and provides for the tax charged in accordance with French legislation to be set off against the tax due in the Netherlands, whereas a parent company is unable to set off tax in the Netherlands in the manner provided for by that convention.**

Unofficial document for media use, not binding on the Court of Justice.

Languages available: ES, CS, DE, EL, EN, FR, IT, HU, NL, PL, SK, SL

The full text of the judgment may be found on the Court's internet site
<http://curia.europa.eu/jurisp/cgi-bin/form.pl?lang=EN&Submit=rechercher&numaff=C-170/05>

It can usually be consulted after midday (CET) on the day judgment is delivered.

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