



## FIELD COURT TAX CHAMBERS

Conference: Withholding taxes in International and European Tax Law,  
University of Luxembourg (25-26 April 2024)

# *Cross-border compensation and neutralisation of discriminatory withholding taxes in European Tax Law*

Rita da Cunha  
Field Court Tax Chambers  
3 Field Court  
Gray's Inn  
London WC1R 5EP  
Tel: 020 3693 3700  
[rdc@fieldtax.com](mailto:rdc@fieldtax.com)



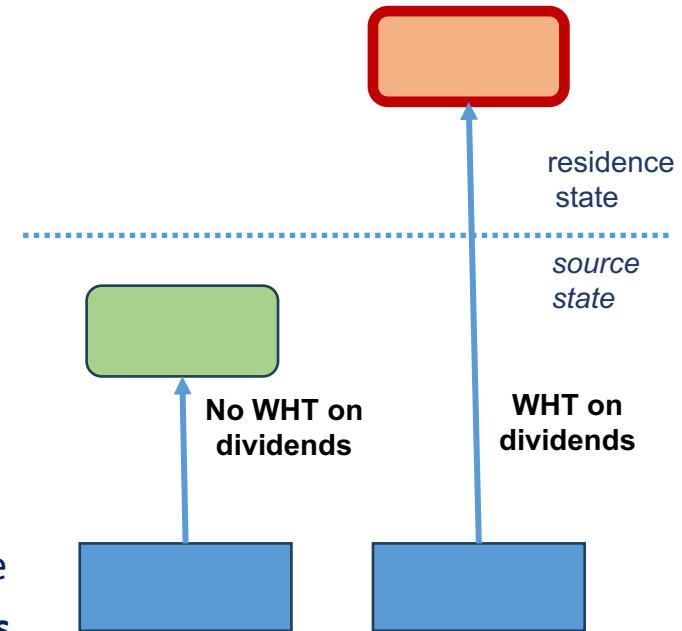
## Introduction

- ◉ The use of the terms “compensation”, “neutralization” and “justification” is not consistent in judgments.
- ◉ It is useful to remember the analysis (steps) followed by the Court of Justice in cases involving the EU fundamental freedoms:
  - 1) Is the national measure discriminatory?
    - What is the relevant/applicable EU freedom?
    - Is there a discrimination or restriction to the exercise of an EU freedom?
    - Is the cross-border transaction / taxpayer in a comparable situation to a domestic transaction / taxpayer (comparability)?
  - 2) Is the discriminatory / unequal treatment justified by an overriding public interest?



## Neutralisation vs compensation (1/2)

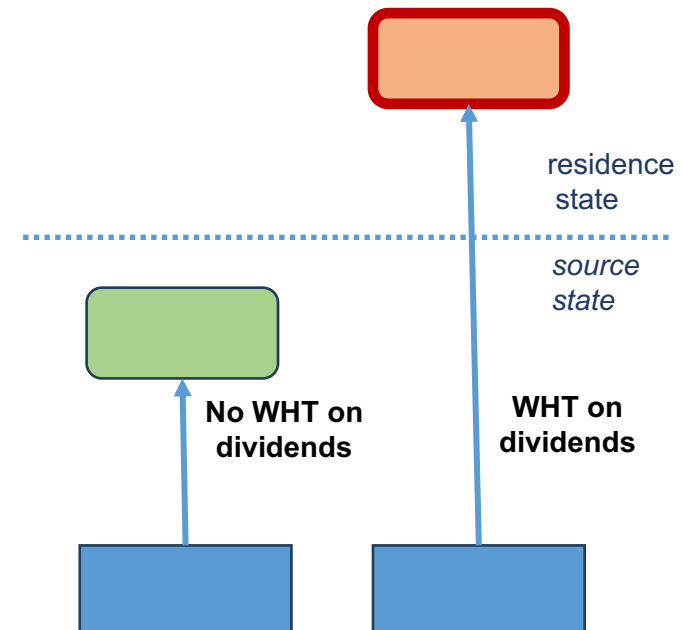
- Neutralisation is concerned with the taxation of the recipient in the residence state:  
For the purposes of assessing whether the levy of a withholding tax by the source state upon cross-border payments effectively results in a discriminatory treatment of the non-resident recipient, **is it relevant how the recipient is taxed on the income in the residence state (full tax credit)?**
- Compensation is concerned with the taxation of the recipient in the source state:  
Whether a source state discriminating against payments made to non-residents (via WHT) may **introduce domestic measures that ensure that the recipient of the income receives equal treatment overall (compensatory mechanisms)?**





## Neutralisation vs compensation (2/2)

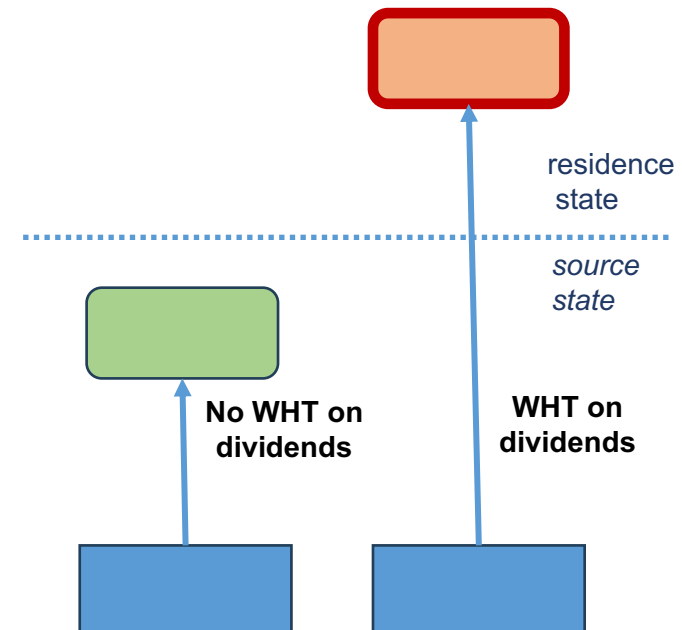
- ⦿ Neutralisation concerned with the taxation of the recipient in the residence state (full tax credit):
  - Leading case: *Amurta* (2007, ECJ, C-379/05), departing from the approach in *Focus Bank* (2004, EFTA Court)
  - Developing *Amurta* approach: *Commission v Italy* (C-540/07); *Commission v Spain* (C-487/08); *Miljoen* (C-10/14, C-14/14 and C-17/14)
- ⦿ Compensation concerned with the taxation of the recipient in the source state (compensatory measures):
  - Issue mentioned in *Amurta* (C-379/05)
  - *Gielen* (C-440/08) and *Beker* (C-168/11)





## Neutralisation of unequal treatment

- ◉ *Amurta* doctrine: Unequal treatment arising from the imposition of a WHT (source state) can **only** be neutralized if the recipient is able to fully deduct a treaty tax credit (as opposed of a full tax credit granted unilaterally by the domestic law of the residence state)
- ◉ Whether the tax treaty enables the effect of the unequal treatment to be neutralized?
  - Tax withheld can be effectively credited in full, regardless of tax treaty provides for a full or partial tax credit: *Miljoen* (C-10/14, C-14/14 and C-17/14)
  - Tax withheld can be effectively credited in full, and the tax treaty provides for a full tax credit: *Commission v Italy* (C-540/07); *Commission v Spain* (C-487/08)





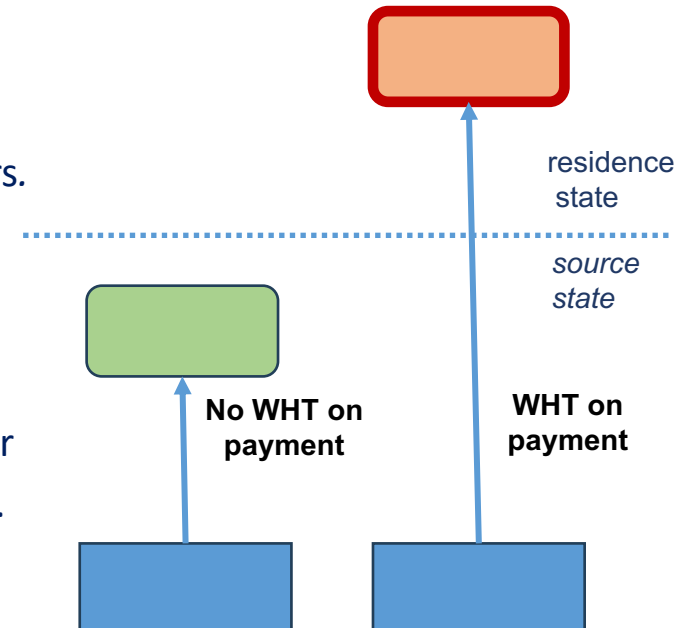
## Compensating unequal treatment

Automatic compensatory measures: The source state makes the application of the WHT conditional on the existence of a treaty that allows the amount withheld to be fully credited in the residence state?

RC: Possibility admitted in *Amurta* + unequal treatment disappears.

Compensatory measures upon request: What if the source state establishes that, if no treaty (full) credit is available in the residence state, the non-resident may apply for a refund? RC: unfavorable treatment is not compatible with EU because of other advantages; cash-flow disadvantage = unequal treatment persists.

Optional compensatory measures: Can the source state compensate for unequal treatment by allowing the non-residents to opt for resident taxation? RC: ECJ rejected optional tax regimes for non-residents as a mean for compensating unequal treatment in *Gielen* (C-440/08) and *Beker* (C-168/11).





## Legal and policy analysis

- ⦿ Case-law regarding the neutralisation of unequal treatment: consistency?
- ⦿ Case-law regarding the compensation for discriminatory WHT: still developing?
- ⦿ Neutralisation and compensation raise issues that clarify the concept of discrimination for the purposes of EU fundamental freedoms, the extent to which EU law conditions the exercise of taxing power by Member States, and what Member States are required to do to ensure compliance with obligations deriving from EU law.
- ⦿ Policy: By narrowing the scope for neutralization and compensation of discriminatory / restrictive effects arising from the imposition of WHT on non-residents, the Court of Justice shows its willingness to protect the internal market.



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*Thank you*

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