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Towards a Stricter Comparability Test

An EU Law Analysis of the Swedish Dividend Withholding Tax Regime in Relation to Non-EU Investment Funds

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Abstract

The aim of this paper is to investigate if it is compatible with the free movement of capital (Article 63 TFEU) to levy a withholding tax on Swedish-sourced dividends paid to non-EU investment funds with legal personality (in the paper referred to as *investment companies*). This question is of relevance since several Swedish intermediaries do not pay any income tax on dividends, either due to a formal tax exemption or to de facto practice. As such, it is clear from CJEU case law that non-EU investment companies should also be exempt from withholding tax on dividends, provided that they are in an objectively comparable situation with any of these Swedish entities and that no justification ground is applicable.

The conclusion of the thesis is that there are indications of that the current Swedish lower court practice, which is to deny comparability between non-EU investment companies and Swedish tax-exempt investment funds with reference to that the foreign entities have a different legal form, is contrary to EU law. Alternatively, it is possible to find discriminatory treatment when comparing the dividend tax treatment of a non-EU investment company with the dividend tax treatment of a Swedish fiscal investment enterprise (*investmentföretag*). For this reason, it is welcome that leave to appeal was recently granted by the Supreme Administrative Court of Sweden in one of the lower court cases dealing with this issue.

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Uppsala, the 4th of June 2019

Fredrika Wendleby

List of Abbreviations

ACD – Authorised Corporate Director

AG – Advocate General

AIFM Directive – Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010

CIV – Collective Investment Vehicle

CJEU – Court of Justice of the European Union

Commission – The European Commission

Court of Appeal – The Administrative Court of Appeal of Sundsvall (*Kammarrätten i Sundsvall*)

DTC – Double Tax Convention

EC – European Community

EU – European Union

FSA – The Swedish Financial Supervisory Authority (*Finansinspektionen*)

IBFD – International Bureau of Fiscal Documentation

ITA – Income Tax Act (*Inkomstskattelagen (SFS 1999:1229)*)

National Board – The National Board on Advance Tax Rulings (*Skatte-rättsnämnden)*

OEIC – Open-Ended Investment Company

PE – Permanent Establishment

RIC – Regulated Investment Company

SAC – The Supreme Administrative Court of Sweden (*Högsta förvaltnings-domstolen*)

SICAV – Societé d'Investissment à Capital Variable

Swedish AIFM Act – Swedish Alternative Investment Funds Managers Act (*Lag (SFS 2013:561) om förvaltare av alternativa investeringsfonder*)

TFEU – The Treaty on the Functioning of the European Union

UCI – Undertaking for Collective Investment

UCITS – Undertakings for Collective Investment in Transferable Securities

UCITS Directive – Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)

UK – The United Kingdom

US – The United States

WTA – The Withholding Tax Act on Dividends (*Kupongskattelagen (SFS 1970:624))*

1. Introduction

1.1 Background

It follows from well-established case law of the Court of Justice of the European Union (CJEU) that it is contrary to the free movement of capital (Article 63 of the Treaty on the Functioning of the European Union (TFEU)) to levy a withholding tax on dividends to non-resident institutional investors in cases where resident institutional investors are exempt from income tax on dividends, provided that the entities are in comparable situations and that no justification ground is applicable.[1] In relation to investment funds, the comparability issue has been identified by scholars as the most difficult issue to address when assessing a dividend withholding tax regime's compatibility with EU law.[2] This issue is particularly complex in relation to investment funds since the legal form, regulation, and taxation of such funds vary greatly from country to country, enabling different interpretations as to what the relevant comparability factors should be.[3]

In Sweden, there is a substantial amount of lower court case law related to the question of comparability in withholding tax situations of foreign investment funds with Swedish investment funds subjected to favourable tax treatment.[4] In the initial cases delivered, an overall assessment of the regulation and structure of the foreign investment fund was used as a basis for the comparability analysis.[5] However,

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[1] See e.g. Case C-303/07 *Aberdeen Property Fininvest Alpha (Aberdeen)* [2009] EU:C:2009:377, Case C-387/11 *Commission v Belgium* [2012] EU:C:2012:670, Case C-190/12 *Emerging Markets Series of DFA Investment Trust Company* (*Emerging Markets)* [2014] EU:C:2014:249, and Case C-480/16 *Fidelity Funds and Others (Fidelity Funds)* [2018] EU:C:2018:480.

[2] See e.g. Viitala and Kujanpää, 'Taxation of Non-Resident Institutional Investors in Finland – Recent Case Law and Developments', *Derivatives and Financial Instruments,* Journals IBFD, 5(20) 2018 sec 1 and Genta, 'Dividends Received by Investment Funds: An EU Law Perspective – Part 2', *European Taxation,* Journals IBFD, 53(4) 2013 p 143.

[3] Viitala and Kujanpää (n 2) sec 1 and Genta (n 2) p 143.

[4] See e.g. the Administrative Court of Appeal of Sundsvall judgments delivered on the 15th of December 2014 in case 863-13, on the 15th of June 2015 in cases 665–669-14, and on the 14th of May 2018 in case 630–632-14.

[5] See e.g. the Administrative Court of Appeal of Sundsvall judgments delivered on the 24th of January 2013 in case 863-13 and on the 15th of June 2015 in case 665–669-14.

recent judgments from the Administrative Court of Appeal of Sundsvall (*Kammarrätten i Sundsvall,* hereinafter: the Court of Appeal) and the National Board on Advance Tax Rulings (*Skatterättsnämnden*, hereinafter: the National Board) demonstrate a shift towards treating the *legal form* of the foreign investment fund as a sole decisive factor.[6] In these two judgments, the foreign investment funds in question are not considered to be in comparable situations with Swedish investment funds on the sole basis that the former, and not the latter, are legal persons.[7] Due to this lack of comparability, the withholding taxes levied on dividends to the foreign investment funds were deemed to be compatible with EU law.

These judgments must be seen in the light of three rulings from the Supreme Administrative Court of Sweden (*Högsta förvaltningsdomstolen,* hereinafter: the SAC), in which the Court has stated that foreign investment funds with legal personality are not in comparable situations with Swedish tax-exempt investment funds, unless they are regulated by the so-called UCITS Directive.[8] While these latter cases deal with the income taxation of the investors of foreign investment funds, and are thus unrelated to the issue of withholding tax, the Swedish Tax Agency (*Skatteverket*), and now the National Board and the Court of Appeal, take the view that the same reasoning should be applied in a withholding tax context.[9]

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[6] The National Board judgment delivered on the 30th of October 2017 in case 4-17/D and the Administrative Court of Appeal of Sundsvall judgment delivered on the 14th of May 2018 in case 630–632-14. Both judgments were appealed to the SAC but in the first case the SAC dismissed the appeal on the basis that the conditions for delivering an advance ruling were not satisfied. However, in the second case leave to appeal was granted. See the SAC decision delivered on the 14th of September 2018 in case 6423-17 and the SAC protocol from the 14th of May 2019 in case 3725–3727-18.

[7] The cases concerned a US mutual fund (with tax status as a RIC) and a Luxembourg (non-UCITS) specialised investment fund (SIF) in the form of a Societé d'Investissment à Capital Variable (SICAV).

[8] RÅ 2006 ref 38, HFD 2016 ref 22, and HFD 2018 ref 61. See also Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS). The UCITS Directive will be discussed in more detail in Chapter 2 below.

[9] See the Swedish Tax Agency's Position Statement 'Utländska motsvarigheter till svenska värdepappersfonder och specialfonder', published on the 20th of March 2017, Dnr 131 103422-

For investment funds with legal personality established outside of the EU these new developments have significant consequences, since such investment funds can never fall within the scope of the UCITS Directive.[10] Nevertheless, it is far from certain if it is compatible with Article 63 TFEU, which also applies in relation to third countries, to levy a withholding tax on dividends to non-UCITS investment funds, that satisfy similar regulatory requirements and objectives as Swedish tax-exempt investment funds, on the sole basis that the former have a different legal form. In this context, it can be mentioned that the new Swedish developments have been criticized in international tax law literature, and that leave to appeal was recently granted by the SAC in the Court of Appeal case mentioned above.[11] Moreover, the assessment becomes more complicated when one considers that not only a comparison with Swedish investment funds, but also with the favourably taxed Swedish fiscal investment enterprise (*investmentföretag)*, could possibly entitle a non-UCITS investment fund with legal personality to an exemption from withholding tax.[12]

17/111. This Position Statement can be contrasted to the Swedish Tax Agency's previous Position Statement on the same topic 'Vad avses med utländska investeringsfonder vid tillämpning av inkomstskattelagen, lagen om investeringssparkonto och kupongskattelagen?', published on the 23rd of May 2012, Dnr 131 128777-12/111, where the Agency states that such a legal form requirement would be contrary to EU law. See also the Swedish Tax Agency's Case Commentary 'HFD 2018 ref. 61; fråga om tillämpning av undantaget från kapitalvinstbeskattning vid fusion mellan utländska alternativa investeringsfonder', published on the 31st of January 2019, Dnr 202 54912-19/111.

[10] Article 1(1) of the UCITS Directive states that the directive only applies to UCITS established within the Member States.

[11] For criticism, see O'Donnell and Molitor-March, 'Funds Taxation and the Third-Country Dimension'. In: *Investment Fund Taxation: Domestic Law, EU Law, and Double Taxation Treaties*, 2018. The authors state that "this new line of argument will be overturned in due course as this is contrary to the CJEU case law established to date" see p 141. The leave to appeal only concerns the question of whether the difference in legal form is enough in itself to preclude comparability with a Swedish investment fund, see SAC protocol from the 14th of May 2019 in case 3725–3727-18.

[12] This latter aspect was touched upon briefly in the Administrative Court of Appeal of Sundsvall judgment delivered on the 14th of May 2018 in case 630–632-14.

1.2 Aim

In light of the above, the aim of this paper is to analyse whether it is compatible with EU law to levy a withholding tax on dividends to non-EU investment funds with legal personality (hereinafter referred to as *investment companies*) that satisfy similar regulatory requirements as Swedish tax-exempt investment funds.

To achieve this aim, three questions need to be answered. First, the scope of the free movement of capital (Article 63 TFEU) in relation to third countries must be investigated (the *applicability question*). Second, it must be examined whether a non-EU investment company is treated less favourably and is in an objectively comparable situation with a Swedish tax-exempt investment fund or a favourably taxed Swedish fiscal investment enterprise (the *restriction question*). Third, if a restriction is found, it must be examined whether there are any applicable justification grounds that could still render the levying of withholding tax acceptable – and if the withholding tax levied is proportional in the light of these justification grounds (the *justification question*).

The analysis will primarily focus on the treatment of two foreign investment companies: the US mutual fund and the UK Open-Ended Investment Company (OEIC). The reasons for focusing on these funds will be presented in Chapter 4, but at this stage it should be clarified that in relation to OEICs the focus will be on the treatment of them post-Brexit, since it is only then that they can be classified as non-EU investment funds.

1.3 Delimitations

First, it can be noted that the new developments described above do not only affect non-EU investment companies but also investment companies established within the EU that are not covered by the UCITS Directive.[13] Nevertheless, the choice has been made to focus solely on the treatment of third country investment companies. This choice has been made to make the argumentation of the paper clearer, as slightly different considerations apply under Article 63 TFEU when assessing a non-EU situation in comparison with an intra-EU situation, and to avoid introducing too many fund types into the paper.[14] Moreover, as stated in section 1.1, the new developments have especially negative consequences for non-EU investment companies, as these can never be covered by the UCITS Directive.

Second, this paper is written from the perspective of EU law. This connotes that any "domestic" arguments relating to the scope and applicability of the withholding tax exception that exists in the Withholding Tax Act on Dividends (*Kupongskattelagen (SFS 1970:624)*, hereinafter: the WTA) for foreign investment funds will be disregarded. In this context, it can briefly be mentioned that the interpretation of this provision conducted by the National Board has not only been subject to criticism from an EU law perspective, but also from a purely "domestic" interpretative perspective.[15]

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[13] The National Board judgment delivered on the 30th of October 2017 in case 4-17/D concerned a Luxemburg SICAV (non-UCITS).

[14] For example, some justification grounds may be invoked in a third-country context that cannot be invoked in an intra-EU context, see Chapter 8 below.

[15] See Cornelius and Segerström, 'Kupongskatt på utdelning till utländsk fond – kommentar till ett förhandsbesked' *Svensk Skattetidning,* 4 2018 sec 4.1. The authors state that the interpretation can inter alia be questioned from a systematic standpoint. Moreover, there are passages in Government Bills that imply that the legal form of a foreign fund should not be a decisive factor. In one Government Bill, the Government states that if the FSA has granted permission to a foreign alternative investment fund to market its units to retail investors in Sweden, this should be treated as an indication of that the foreign fund is equivalent to a Swedish special fund for tax purposes, see Government Bill 2012/13:155 p 391. Such a permission is not dependent on the legal form of the foreign fund, see Chapter 4, sec 2 of the Swedish AIFM Act.

Third, the paper will not discuss whether it is possible to make so-called "horizontal comparisons" to find discriminatory treatment in EU law cases dealing with direct taxation. This is despite the fact that horizontal comparisons were discussed by the minority of the National Board as an argument for seeing the majority's ruling as contrary to EU law.[16] The decision has been made to exclude this topic since it is widely discussed in literature whether it is at all possible to rely on a horizontal comparison – that is a comparison with another cross-border situation rather than with an internal situation – to find discriminatory treatment.[17] Moreover, even the scholars that claim that the CJEU relies on horizontal comparisons in its comparability analysis consider it uncertain whether horizontal comparisons can be relied on in a *third country* context.[18] In this respect, it can be mentioned that the National Board ruling concerned an intra-EU situation.

Fourth, it will not be addressed if it is possible to find discriminatory treatment when comparing the dividend tax treatment of a non-EU investment company with the dividend tax treatment of a Swedish company limited by shares. In this regard, it has been pointed out that it should be possible to find less favourable treatment when comparing a foreign investment company with a Swedish company, due to the different tax rates applied on dividends received by these two entities.[19] Nevertheless, in relation to UK OEICs and US mutual funds, a lower tax rate will in any case be applied under the Sweden-UK Double Tax Convention (DTC) or the Sweden-US DTC.[20] As such, the less favourable treatment of these two

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[16] The National Board judgment delivered on the 30th of October 2017 in case 4/17 D.

[17] See for different views Johansson, *EU-domstolens restriktionsprövning i mål om de grundläggande friheterna och direkta skatter,* 2016 p 252–264, Simander, *Withholding Taxes and the Fundamental Freedoms*, 2013 p 157–167 and p 327, Bammens, *The Principle of Non-Discrimination in International and European Tax Law*, 2012 p 874 and Smit, *EU Freedoms, Non-EU Countries and Company Taxation*, 2012 p 518–519.

[18] Smit (n 17) p 519.

[19] Swedish companies are generally taxed on dividends at a rate of 21.4 % under the ITA, whereas non-EU investment companies are subjected to a tax rate of 30 % under the WTA, see Chapter 65, sec 10 of the ITA and sec 5 of the WTA. See also Cornelius and Segerström (n 15) sec 4.2.4.

[20] Article 10 of the Sweden-US DTC stipulates that dividends can be taxed in the source state at a maximum tax rate of 15 % and Article 10 of the Sweden-UK DTC stipulates that dividends can be

subjects is neutralised, even if it was found that they were in objectively comparable situations with a Swedish company limited by shares.[21] For this reason, the choice has been made not to discuss this issue in the paper.

Lastly, it will be assumed that discrimination (less favourable treatment of objectively comparable situations) is necessary for a domestic tax rule to be incompatible with EU law. Nevertheless, in literature some scholars have argued that there may be examples in CJEU case law of that *non*-discriminatory tax rules hindering free movement can also be contrary to EU law.[22] Still, this is a discussion that falls outside the scope of this paper.

1.4 Terminology

In literature, it has been stated that the terminology used when discussing investment funds is very sensitive, as there are different meanings for the concepts used in various national laws and in practice.[23] For this reason, it is important to make certain clarifications.

Initially, what is referred to as an *investment fund* in this paper is often referred to as an Undertaking for Collective Investment (UCI) on a European level.[24] This acronym should therefore be treated as a synonym to the investment fund concept. Here, it can also be stressed that there is no general legal definition of an investment fund, either in Sweden or internationally, but only specific definitions

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taxed at a maximum tax rate of 5 % in the source state. See also para 28 of the Commentary to Article 1 of the *OECD Model Tax Convention on Income and on Capital* regarding that a US mutual fund or a UK OEIC are the "beneficial owners" of a dividend payment.

[21] That applying different tax rates can be considered less favourable treatment follows from Case C-311/97 *Royal Bank of Scotland* [1999] EU:C:1999:216 para 30. See also the Commission, 'Taxation: Belgium before the EU Court of Justice for discriminatory taxation of collective investment undertakings', published on the 16th of October 2014.

[22] See Johansson, (n 17) p 265–266 and Cejie, *Utflyttningsbeskattning av kapitalökningar: en skattevetenskaplig studie i internationell personbeskattning med fokus på skatteavtals- och EU-rättsliga problem*, 2010 p 268–271 for a discussion on this topic.

[23] Riassetto, 'Introduction to Investment Funds Law'. In: *Investment Fund Taxation: Domestic Law, EU Law, and Double Taxation Treaties,* 2018 p 9.

[24] Riassetto (n 23) p 9.

relating to specific types of investment funds (such as UCITS funds).[25] In this paper, the term investment fund will therefore be used for all entities that either fall within the scope of the UCITS Directive or that fulfil the criteria necessary to be qualified as a specific type of investment fund (or a UCI depending on the terms used) under the applicable national law.[26]

Additionally, since the aim of this paper is to investigate whether the Swedish treatment of third country *investment companies* is compatible with EU law, it should be clarified what is meant by an investment company. In this paper, the term will be used to signify an investment fund in the form of a company with variable share capital (the Swedish translation for this fund type is *investeringsbolag*). As we shall see below, this fund form does not exist in Sweden, but some foreign examples are the Luxemburg SICAV (Societé d'Investissment à Capital Variable), the US mutual fund (in tax terms often referred to as a Regulated Investment Company (RIC)), and the UK OEIC. The US mutual fund and the UK OEIC, as well as the terminology connected to these fund types, will be presented more in depth in Chapter 4. Still, it can be noted already at this stage that by "variable share capital" it is meant that the capital of an investment company automatically increases or decreases with subscriptions and redemptions of shares in the company without the need for a formal procedure.[27] This leads to that an investment company's capital is always equal to its net assets.[28]

It should be mentioned that in literature "Swedish investment company" is often used as an alternative translation for the favourably taxed *Swedish fiscal investment enterprise* (the Swedish term being *investmentföretag*).[29] Nevertheless,

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[25] Riassetto (n 23) p 9. The criteria that must be fulfilled for a fund to qualify as a UCITS will be presented in Chapter 2.

[26] Compare Viitala, *Taxation of Investment Funds in the European Union*, 2005 p 13 where a similar approach is used.

[27] Fort and Jost, 'Investment Funds Taxation in Luxemburg'. In: *Investment Fund Taxation: Domestic Law, EU Law, and Double Taxation Treaties,* 2018 p 48.

[28] Fort and Jost (n 27) p 48.

[29] Gunne, 'The Taxation of Investment Funds', *IFA Cahiers,* 82b 1997, and Dahlberg, 'On the Taxation of Swedish Investment Companies', *Scandinavian Studies of Law,* 44 2003.

the concern has been that using the term investment company for this entity would be confusing for the reader when this term is also used to refer to a specific type of investment fund. Therefore, *fiscal investment enterprise* or *investment enterprise* will be used when referring to the favourably taxed entity *investmentföretag,* while *investment company* will be used when discussing investment funds in the form of companies with variable share capital. When both fiscal investment enterprises and investment funds are referred to the term *collective investment vehicles* (CIVs) will sometimes be used.[30]

Lastly, when discussing EU court cases, reference is made to the most recent titles and the currently applicable TFEU articles, even if different terms or article numbers were used when the cases were delivered. For example, EU will be used instead of EC (European Community) and references will only be made to the TFEU and not to previous versions of EU treaties.

[30] For a discussion on the term CIV, see paras 22–48 of the Commentary to Article 1 of the *OECD Model Tax Convention on Income and Capital.* As with the investment fund concept, the CIV concept can have various meanings in different jurisdictions.

1.5 Method and Material

The paper will rely on the legal method known as the "legal dogmatic method" (*rättsdogmatisk metod*) in Sweden, with some elements of a comparative method. By "legal dogmatic method", it is meant that the paper will use Swedish legal sources to describe what the position of the law is in relation to the research question.[31] Since this is a paper on EU law, the primary legal source used is CJEU case law. Nevertheless, initially some sources that are not typically granted the force of law, such as case law from lower courts (the National Board and the Court of Appeal) and position statements from the Swedish Tax Agency, will also be discussed in the paper. However, these sources are primarily used as a basis for the analysis of CJEU case law and not for any conclusions as to what the law states as such.[32]

Part of the analysis will also rely on a comparison between Swedish tax-exempt investment funds and certain non-EU investment companies. For this reason, it has been necessary to find information on how these foreign investment companies are regulated and taxed in the states where they are established. Here, it has been necessary to rely on secondary information, as the author cannot claim to have any in depth knowledge of the investment fund legislation of the jurisdictions looked at (namely the UK and the US). In this context, the Global Legal Group's *International Comparative Legal Guide to Public Investment Funds* has been relied on to a large extent when it comes to the regulation of the foreign investment

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[31] See Kleineman,'Rättsdogmatisk metod'. In: *Juridisk metodlära*, 2018 p 21–24 for a presentation of the "legal dogmatic method".

[32] Compare Påhlsson, *Konstitutionell skatterätt,* 2018 p 105–117 where he discusses that the position statements are at least useful as indications of de facto administrative practice. See also, Reichel, 'EU-rättslig metod'. In: *Juridisk metodlära*, 2018 p 109–142 for a presentation of the method used by the CJEU when applying EU law (the "EU legal method" (*EU-rättslig metod*)). In the author's view, this method falls within the scope of the "legal dogmatic method", since it is also used to find out what the position of the law is. For this reason, it is not discussed as a separate method in this section.

funds.[33] Apart from this comparative legal guide, secondary information has been obtained from the International Bureau of Fiscal Documentation's (IBFD) Topical Analyses on "Investment Funds & Private Equity", as well as the IBFD's Country Analyses on the US and the UK, specifically the sections dealing with "Taxation of Special Types of Entity". The Topical Analyses deal with both the regulation and taxation of the foreign fund types, whereas the Country Analyses only deal with taxation.

All the secondary information used has been updated either 2017 or 2018, and it is therefore assumed that the legislation presented is still in force. However, the primary legal sources of the UK and the US have not been looked at and rapid developments tend to take place in investment fund legislation, which could lead to that some of the information used may no longer be accurate. Nevertheless, by applying and cross-checking three separate secondary sources it is at least the author's intent that the paper should accurately describe the regulation and taxation of these fund types as it existed in 2018.

The selection of CJEU case law for closer study was made by looking at a list compiled by the European Commission (hereinafter: the Commission) named "CJEU cases in the area of, or of particular interest for, direct taxation", updated on the 1st of April 2018. First, all the cases on this list with the key words "dividends", "funds", "investment funds", "investment companies", or "UCITS" were looked at more closely. Second, an additional search was conducted in the EUR-Lex database to see if any new cases on dividend taxation of interest for the paper had been delivered after the 1st of April 2018.[34]

[33] Global Legal Group, *The International Comparative Legal Guide to Public Investment Funds,* 2018. This legal guide contains contributions from law firms in several countries that specialize in the regulatory requirements of investment funds.

[34] The only such case found was the case *Fidelity Funds* (n 1). See also the Commission, 'CJEU cases in the area of, or of particular interest for, direct taxation', updated on the 1st of April 2018.

1.6 Previous Research Conducted on the Topic

From the perspective that the Swedish developments regarding withholding taxes and investment funds have even been observed in international tax literature, it can be argued that there is surprisingly little written on this topic in Sweden. The dividend taxation of investment funds from an EU law perspective has not been the focus of any Swedish doctoral thesis or research study, to the author's knowledge, and most of the literature on comparability of foreign investment funds with Swedish tax-exempt investment funds can be traced back to 2012, when the exception from withholding tax for foreign investment funds was first introduced in the WTA.[35] In this regard, some scholars at the time took the view that a legal form requirement would be contrary to EU law, which also corresponds to the Swedish Tax Agency's view at the time.[36] Nevertheless, the only article that the author has managed to find on the new developments – where legal form has been introduced as a decisive factor in the comparability analysis – is rather short and written by practitioners at a tax law firm.[37] Arguably, this is likely to change in the future since the SAC, as mentioned in section 1.1, recently granted leave to appeal in one of the cases dealing with this issue.[38]

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[35] It can be admitted that Dahlberg has discussed the capital gains taxation of investment funds, see Dahlberg, *Ränta eller kapitalvinst*, 2011 p 68–75. The most important contribution when it comes to dividend taxation and investment funds is probably the anthology *Reglering och beskattning av investeringsfonder* from 2012 where Dahlberg, Dufwa, and Lohela write about the taxation of investment funds in the light of EU law. The withholding tax exception in the WTA will be explained in section 3.5 below.

[36] See the Swedish Tax Agency's Position Statement published on the 23rd of May 2012 (n 9). This view is expressed, inter alia, by Lohela in Lohela, 'Investeringsfonder – EU-skatterättsliga och skatteavtalsrättsliga synpunkter'. In: *Reglering och beskattning av investeringsfonder,* 2012 p 50–51 and by Dahlberg, see Dahlberg, 'Investeringsfonder och beskattning – nya problem med förändrad lagstiftning'. In: *Reglering och beskattning av investeringsfonder,* 2012 p 23–24. In Dahlberg's case, this is expressed by that he states that the considerations put forward in the previous Swedish Tax Authority's Position Statement (including what is stated in it on legal form) are reasonable and well-founded. Both Lohela and Dahlberg are members of the National Board and Lohela sided with the majority in the National Board judgment mentioned in section 1.1, which suggests that she has changed her mind, while Dahlberg sided with the minority. It can be noted that Lohela works at the Swedish Tax Agency (both now and in 2012).

[37] Cornelius and Segerström (n 15).

[38] Leave to appeal was granted on the 14th of May 2019, see the SAC protocol from the 14th of May 2019 in case 3725–3727-18.

Conversely, dividend taxation of investment funds from an EU law perspective has been the focus of a doctoral thesis abroad: Tomi Viitala's *Taxation of Investment Funds in the European Union*.[39] In this doctoral thesis, EU fundamental freedoms and their implications for the taxation of investment funds are the explicit focus of one of the chapters.[40] However, the thesis was published in 2004, that is before the first CJEU case on investment funds and withholding taxes had been published.[41] For this reason, the thesis mostly discusses whether the levying of withholding tax on dividends to foreign investment funds can be precluded by EU law at all, and the question of comparability is not discussed in detail.[42] Nevertheless, Viitala has since then also commented on some of the CJEU investment fund cases addressed in the paper.[43]

The question of comparability of foreign investment funds with domestic investment funds is also briefly discussed in Daniël Smit's doctoral thesis *EU Freedoms, Non-EU Countries and Company Taxation* from 2011. Smit states that the comparability of foreign investment funds with domestic investment funds is hard to assess based on the CJEU case law that existed at the time. Nonetheless, he states that in his view the relevant comparability factors should be assessed "on the basis of the underlying rationale of the contested tax regime".[44] Legal form as such is not explicitly addressed.

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[39] See also Adema, *UCITS and Taxation: Towards Harmonization of the Taxation of UCITS,* 2009 for a de lege ferenda perspective on how the taxation of UCITS could be harmonised within the EU. This study is not discussed in detail since negative integration through EU law is not its focus.
[40] Viitala (n 26) p 262–268.
[41] Viitala expressly states that there is no case law on the topic at the time when the thesis is written, see Viitala (n 26) p 205.
[42] Viitala (n 26) p 265–268. Viitala answers this question in the affirmative: "Community law /…/ prevents a Member State from applying a withholding tax on income paid to a foreign investment fund established in another Member State, if, at the same time, domestic investment funds are exempt from taxes", see Viitala (n 26) p 268.
[43] Viitala, 'Comparability of Different CIVs under EU Law'. In: *The Tax Treatment of CIVs and REITs*, 2013 p 147–160.
[44] Smit (n 17) p 516.

Additionally, several other international scholars have written articles on EU fundamental freedoms and investment funds, and discussions on this topic can also be found in anthologies dealing with the taxation of investment funds.[45] Still, to the author's knowledge, the most recent judgment delivered by the CJEU in relation to investment funds and withholding tax, *Fidelity Funds,* has neither been studied in depth in Swedish nor international tax law literature.[46]

Lastly, it can be mentioned that more general doctoral theses on EU fundamental freedoms and direct taxation can be found both in Sweden and abroad. Since the amount of such theses is great, it will not be possible to reference to all of them. However, a recent Swedish example of interest for this paper is Jesper Johansson's *EU-domstolens restriktionsprövning i mål om de grundläggande friheterna och direkta skatter* from 2016. Additionally, some foreign examples of doctoral theses of relevance are Karin Simander's *Withholding Taxes and the Fundamental Freedoms* from 2013 and Niels Bammens' *The Principle of Non-Discrimination in International and European Law* from 2011. While neither of these publications explicitly discuss investment funds, they are interesting since general aspects of the CJEU's comparability analysis are addressed in them, such as whether it is possible to take more than one taxable entity into account when conducting a comparability analysis.

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[45] For chapters in anthologies, see Viitala (n 43), O'Donnell and Molitor-March (n 11), and Tenore, 'Investment Fund Taxation and Fundamental Freedoms: Four Approaches to Comparability'. In *Investment Fund Taxation: Domestic Law, EU Law and Double Taxation Treaties*, 2018. For articles on investment funds, see e.g. Genta, (n 2), and Hippert, 'The TFEU Eligibility of Non-EU Investment Funds Subjected to Discriminatory Dividend Withholding Taxes', *EC Tax Review*, 2 2016.

[46] On the Case information page, the only articles listed under "Academic writings" are one article written in Dutch and one article written in German, see Curia, 'Judgment of the Court of 21 June 2018 in Case C-488/16: Case information'. Moreover, a search in the IBFD database, as well as on Zeteo and Karnov, rendered no more than short summaries of the case.

1.7 Structure

To understand the reasoning and conclusions of this paper, it is important to have a basic understanding of the regulation, structure, and taxation of investment funds and fiscal investment enterprises. For this reason, Chapter 2 of the paper deals with the definition, regulatory framework and legal structure of Swedish investment funds, whereas Chapter 3 deals with the taxation of Swedish investment funds and fiscal investment enterprises, as well as the withholding tax rules applicable for third country investment funds.[47] In this latter chapter, the background to the tax provisions is also discussed, as the CJEU has stated that the purpose of a regulation is relevant in the assessment of comparable situations.[48] Chapters 2 and 3 are of a general character, and for readers that are already well-acquainted with the regulation and taxation of Swedish investment funds, it is possible to skip ahead to Chapter 4 directly. In Chapter 4, a presentation is made of some foreign investment companies, which then serves as a basis for the subsequent analysis.

Thereafter, the scope of the free movement of capital in relation to third countries is analysed (Chapter 5), followed by an examination of case law (Chapters 6-8). First, Swedish case law on withholding taxes on dividends to foreign investment companies will be examined (Chapter 6). The recent case law discussed in the Introduction will be contrasted to older Swedish case law, to demonstrate the shift that has occurred in the assessment of comparable situations. After this, CJEU case law is discussed and analysed (Chapters 7-8). The analysis is divided into two chapters: one that deals with the so-called "restriction test" and one that deals with the so-called "justification test".[49] The conclusions of the analysis are summarized in a final chapter (Chapter 9).

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[47] Since fiscal investment enterprises are organised as "normal" companies limited by shares (*aktiebolag*) or as cooperatives (*ekonomiska föreningar*) it has not been considered necessary to discuss the civil law aspects or the regulatory framework of investment enterprises.

[48] See e.g. Case C-252/14 *Pensioenfonds Metaal en Techniek* (*PMT*) [2016] EU:C:2016:402 para 48 and *Fidelity Funds* (n 1) para 50.

[49] See more about the different tests in section 6.1 below.

2. Definitions and Regulatory Framework of Swedish Investment Funds

2.1 Introduction

In the Government Bill implementing the Income Tax Act (*Inkomstskattelagen (SFS 1999:1229*), hereinafter: the ITA) it is stated that there is no special tax definition for the different forms of Swedish investment funds and that recourse must therefore be had to civil or economic law (*civil- eller näringsrättslig lagstiftning*) for the purpose of finding such definitions.[50] In this chapter, civil and economic law will therefore be used to explain the different investment fund types that exist in Sweden.

In this regard, civil and economic law differentiates between three groups of Swedish investment funds: UCITS funds (*värdepappersfonder*), special funds (*specialfonder*), and alternative investment funds (*alternativa investerings-fonder*).[51] As we shall see in Chapter 3 below, only UCITS funds and special funds are subjected to a special tax regime. However, in order to understand the analysis and reasoning of the subsequent chapters, it is also necessary to understand what is meant by an alternative investment fund. Consequently, the regulatory framework and structure of all three investment fund types will be presented in this chapter.

[50] Government Bill 1999/2000:2 (part 2) p 453.
[51] Wendleby and Renström Secka, 'Sweden'. In: *The International Comparative Legal Guide to Public Investment Funds*, 2018 p 109.

2.2 Swedish UCITS Funds and Swedish Special Funds

Swedish UCITS funds are regulated by the Swedish UCITS Act (*Lag (SFS 2004:46) om värdepappersfonder*), which is modelled on the UCITS Directive. UCITS is short for Undertakings for Collective Investment In Transferable Securities and the aim of the UCITS Directive is to remove restrictions on the free movement of such undertakings' units within the EU.[52] To achieve this aim, the Directive establishes common basic rules regarding the authorization, supervision, structure, and activities of investment funds in order for them to qualify as a UCITS.[53] If an investment fund satisfies these requirements, and is subsequently authorized as a UCITS fund in one Member State, the fund may market its units in any other Member State, subject to certain notification requirements.[54]

In order to qualify as a UCITS, the sole object of the fund must be collective investment in transferable securities or in other liquid financial assets through capital raised from the public.[55] Moreover, the fund must be open-ended, connoting that the units of UCITS funds must be redeemed or repurchased at the request of the unitholders.[56] Additionally, a UCITS fund must operate the principle of risk spreading.[57] As an example of this, a UCITS fund cannot normally invest more than 5 % of its assets in transferable securities or money market instruments issued by the same body.[58]

According to the UCITS Directive, a UCITS fund can be established in accordance with contract law (as common funds managed by management companies), trust law (as unit trusts – this fund form typically only exists in

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[52] Recital no 3 of the Preamble to the UCITS Directive.
[53] Recital no 4 of the Preamble to the UCITS Directive.
[54] Article 91 of the UCITS Directive. See also chapter 1, secs 6–11 of the Swedish UCITS Act regarding the reciprocity principle.
[55] Article 1(2) of the UCITS Directive and Chapter 1, sec 1, para 25 of the Swedish UCITS Act.
[56] Article 1(2) of the UCITS Directive and Chapter 1, sec 1, para 25 of the Swedish UCITS Act.
[57] Article 1(2) of the UCITS Directive and Chapter 1, sec 1, para 25 of the Swedish UCITS Act.
[58] Article 52(1)(a) of the UCITS Directive and Chapter 5, sec 6 of the Swedish UCITS Act. There are some exceptions to these rules, see Chapter 5, sec 6, subs 2 of the Swedish UCITS Act.

common law jurisdictions), or statute (as investment companies with variable share capital).[59] However, the Swedish UCITS Act only allows for the contractual form.[60] The reason for this is primarily that Swedish company law does not allow for the establishment of companies with variable share capital, which would be necessary if a Swedish company were to comply with the open-ended fund requirements of the UCITS Directive.[61]

The legal structure of a Swedish UCITS therefore builds on a contractual relationship between the owners of a fund (the unitholders), a fund management company, and an authorised depositary. The fund itself is not a legal person and it is the task of the fund management company to act in the interest of the unitholders – who each owns a proportion of the fund – and represent the unitholders in all matters concerning the fund.[62] For safekeeping purposes, the UCITS fund (consisting of the fund assets) is held by an authorised depositary, which is typically a bank.[63] The depositary also performs a control function in the sense that it monitors that the fund management company complies with the UCITS Act and the fund rules (*fondbestämmelser*).[64] Both the management company and the depositary receives a fee from the fund for the performance of their activities, and both of these entities are supervised by the Swedish Financial Supervisory Authority (*Finansinspektionen,* hereinafter: the FSA).[65]

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[59] Article 1(3) of the UCITS Directive. That unit trusts can typically only be found in common law jurisdictions follows from Staberg, 'Utländska motsvarigheter till svenska investeringsfonder', *Skattenytt,* 2008 p 101.

[60] Chapter 4, sec 1 of the Swedish UCITS Act.

[61] SOU 2016:45 p 217 and SOU 2002:56 p 520–521. It is stated that as long as specific decisions at a general shareholder meeting are required to increase or decrease the share capital, it will not be possible for a Swedish company to redeem or repurchase shares every day, which is a UCITS requirement. Here it can be mentioned that the possibility of introducing companies with variable share capital into Swedish company law has been investigated several times, see SOU 2016:45 and SOU 2002:56.

[62] Chapter 4, sec 2 of the Swedish UCITS Act.

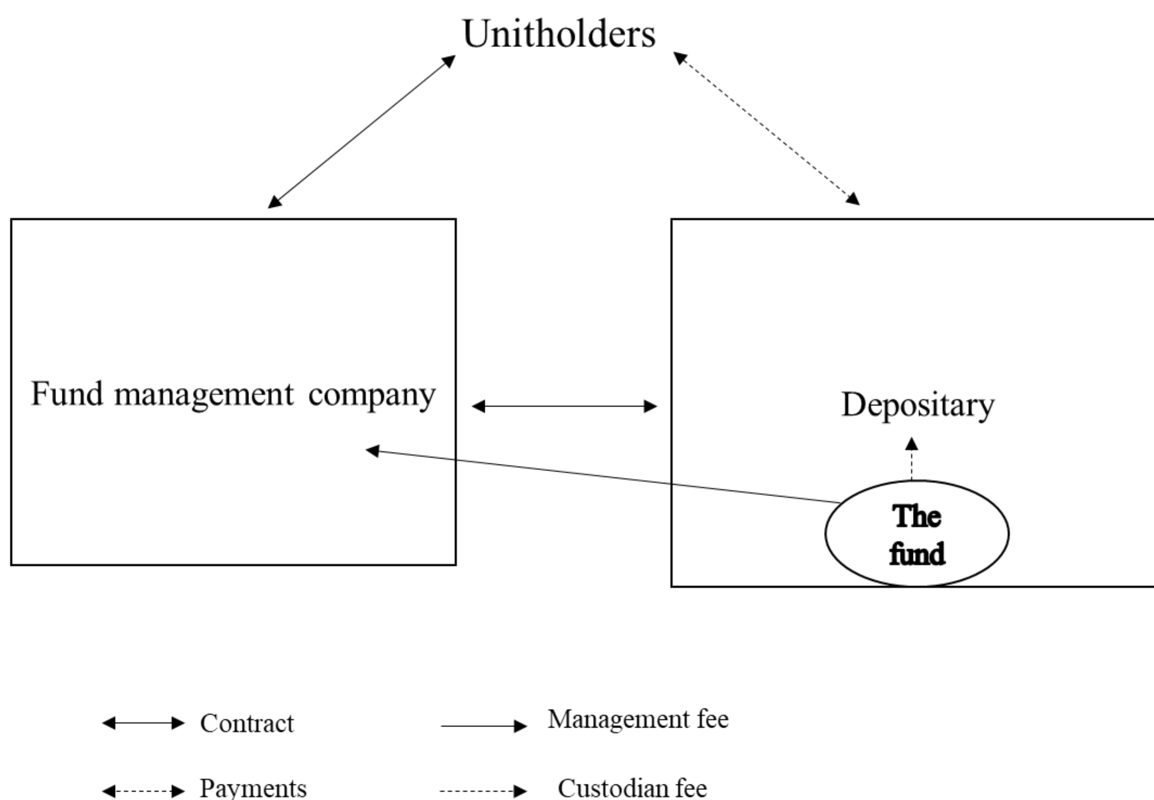
[63] Chapter 3, sec 1 of the Swedish UCITS Act and Government Bill 2012/13:155 p 175.

[64] Chapter 3, sec 4 of the Swedish UCITS Act.

[65] Adema (n 39) p 13–14. See also Chapter 10, sec 1 of the Swedish UCITS Act. That a depositary and management company of a UCITS fund has to be subject to supervision by a competent authority follows from the UCITS Directive, see Article 6(2), Article 23(2) and Article 33(2) of the UCITS

Special funds are organised in the same way as UCITS funds (i.e. they are established in the contractual form, see diagram 1 below) and are basically subject to the same regulatory requirements and supervision, with some important exceptions.[66] To give some examples, the portfolio of a special fund can be less diversified (subject to the approval of the FSA), the special fund can be directed towards a limited group of investors instead of the general public, and there can be restrictions on the possibility to redeem fund units.[67] Still, a special fund must be open for redemption at least once a year.[68]

Diagram 1 – The structure of a Swedish UCITS fund and Swedish special fund (contractual fund)[69]



Directive. The Swedish competent authority under the UCITS Directive is the FSA (compare Article 97 of the UCITS Directive).

66 See Chapter 12 of the Swedish AIFM Act where special funds are regulated.

67 Chapter 12, sec 4, Chapter 12, sec 6, and Chapter 12, sec 13 of the Swedish AIFM Act.

68 Chapter 12, sec 6 of the Swedish AIFM Act.

69 This illustration has been inspired by an illustration in Government Bill 2012/13:155 p 175 and by an illustration in Adema (n 39) p 14.

2.3 Alternative Investment Funds

Alternative investment funds are regulated by the Swedish Alternative Investment Funds Managers Act (*Lag (SFS 2013:561) om förvaltare av alternativa investeringsfonder*, hereinafter: the Swedish AIFM Act), which is modelled on the AIFM Directive.[70] According to the AIFM Directive and the Swedish AIFM Act, an alternative investment fund is a fund that raises capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors, and which does not fall within the scope of the UCITS Directive.[71] In this respect, it can be noted that a special fund fulfils these conditions and can therefore be categorised as an alternative investment fund. However, due to that a special fund must also fulfil certain additional requirements, the choice has been made to present this fund form together with UCITS funds above.

The AIFM Directive, as well as the Swedish AIFM Act, does not regulate the alternative investment funds themselves (except for special funds in the case of the Swedish AIFM Act), but the managers of the funds.[72] This entails that there are no limits on portfolio investments or legal form requirements for other alternative investment funds than special funds. In other words, an alternative investment fund can either be established in the contractual form – in the same way as a UCITS fund or special fund – or have legal personality and be organised as, for example, a Swedish company limited by shares.[73] All alternative investment funds organised as a company are closed-ended, connoting that shareholders of such companies cannot rely on the company to redeem or repurchase shares at request, but that the shares can only be sold at a secondary market. As stated above, this is due to that

[70] Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010.

[71] Article 4(1)(a) of the AIFM Directive and Chapter 1, sec 2 of the Swedish AIFM Act.

[72] Article 1 of the AIFM Directive and Chapter 1, sec 1 of the Swedish AIFM Act.

[73] SOU 2016:45 p 217.

Swedish company law does not allow for companies to issue new shares or withdraw shares on redemption without the need for a formal procedure.[74] In contrast to unitholders of a contractual fund, shareholders of an alternative investment fund with legal personality do not own a proportion of the fund itself, but shares in the company that gives them certain legal rights towards the fund.[75]

Lastly, it should be mentioned that an alternative investment fund that is not a special fund can only be offered to the public if it has been admitted to trading on a regulated market.[76] Alternative investment funds are therefore, in contrast to UCITS funds and special funds, directed towards professional investors instead of the general public as a main rule, which explains why rules on consumer protection (e.g. strict rules on risk diversification and eligible assets) are missing for these funds.[77]

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[74] SOU 2002:56 p 167.

[75] This follows from the Swedish Companies Act (*Aktiebolagslagen (SFS 2005:551)*), see e.g. Chapter 4, sec 4 of the Act.

[76] Chapter 4, sec 4 of the Swedish AIFM Act.

[77] Government Bill 2012/13:155 p 176. Professional investors are, for example, banks and financial institutions, companies that satisfy certain capital or turnover requirements and government agencies, see Chapter 1, sec 11, para 21 of the Swedish AIFM Act which in turn references to Chapter 9, secs 4–5 of the Swedish Financial Markets Act (*Lag* (*SFS 2007:528*) *om värdepappersmarknaden*).

3. The Taxation of Fiscal Investment Enterprises and Investment Funds

3.1 Definition of a Swedish Fiscal Investment Enterprise

Above, different types of Swedish investment funds have been presented. However, the fiscal investment enterprise concept has not been touched upon in detail. The reason for this is that this concept does not, unlike tax-exempt investment funds, depend exclusively on any civil law or economic law definition. Instead, this is a concept constructed entirely for tax purposes.

According to the ITA, a fiscal investment enterprise is a Swedish company limited by shares or a Swedish cooperative, with a great number of individual shareholders, that exclusively or almost exclusively manages securities and whose principal object is to achieve risk diversification by maintaining a diversified portfolio of securities.[78] It has been stated in literature that these criteria, apart from the criterion of being a Swedish company limited by shares or a Swedish cooperative, have been inserted with the purpose of placing investment enterprises on the same level as UCITS funds and special funds.[79] The criteria make sure that investment enterprises are, just as UCITS funds and special funds, primarily used for collective investment by ("ordinary") individual investors, and that similar consumer protection is achieved through risk diversification and by principally investing in liquid assets.[80] In practice, the requirement that a company needs to have a great number of individual shareholders to qualify as an investment enterprise has led to that all Swedish investment enterprises are listed at the Stockholm Stock Exchange.[81]

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[78] Chapter 39, sec 15 of the ITA.
[79] Dahlberg (n 29) p 104.
[80] Dahlberg (n 29) p 104.
[81] See Gunne (n 29) p 778.

3.2 Taxation of Swedish Fiscal Investment Enterprises

Between 1990 and 2012, Swedish investment enterprises, special funds, and UCITS funds were regulated in the same manner for tax purposes.[82] The same tax treatment still applies for investment enterprises and shall be explained in this section. However, first it can be noted that the previous legislation applicable for Swedish UCITS funds and Swedish special funds did not refer to these fund types per se, but to "Swedish investment funds". The background to this was that at the time when the legislation was enacted, the concept of alternative investment fund had not been introduced into the Swedish legislation. Consequently, only Swedish UCITS funds and special funds were regarded as "Swedish investment funds".[83]

It can be held that the Government's main reason for enacting special rules for investment funds and investment enterprises in the first place was that such entities are mere *intermediaries* for collective investment in securities.[84] For this reason, it was considered necessary to achieve three legislative objectives when taxing these entities:

- neutrality between direct and indirect investment (referred to in literature as the principle of transparency),[85]
- that different forms of intermediaries should be treated in the same way for tax purposes, and
- that it should be simple for the intermediaries to make portfolio adjustments.[86]

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[82] Government Bill 1989/90:110 p 559–566.
[83] Government Bill 1989/90:110 p 560. This is important to note for the discussion in section 7.4.5.
[84] Government Bill 1989/90:110 p 564.
[85] Adema (n 39) p 1 and Viitala (n 26) p 50. Adema states that according to this principle the tax burden for investments by way of collective investment vehicles should not be greater or lesser than the tax burden for direct investments. In the Government Bill, the purpose that indirect investment should not be treated *more* favourably than direct investment is treated as an aim separate from the aim of achieving neutrality between direct and indirect investment. However, in the author's view it makes sense to refer to these aims together since they are two sides of the same coin (the coin being the principle of transparency). See Government Bill 1989/90:110 p 564.
[86] Government Bill 1989/90:110 p 564.

To achieve these aims, several special rules were enacted that still apply for investment enterprises.[87] However, for the purposes of this paper, it is only necessary to focus on the rules inserted by the Government to reach the first objective (the principle of transparency). To meet this objective, the Government inserted a possibility for fiscal investment enterprises to deduct dividends paid to their shareholders.[88] In principle, this leads to that an investment enterprise generally does not pay any income tax, including income tax on dividends received.[89] This is the case since a dividend matching the taxable income for a certain fiscal year is typically calculated and distributed to the shareholders of the investment company, resulting in that the taxable income is "rolled over" on them.

3.3 Taxation of Swedish UCITS Funds and Special Funds

In 2012, new legislation was enacted for UCITS funds and special funds, making them tax-exempt.[90] In light of the second legislative objective mentioned in section 3.2 above – that different forms of intermediaries should be treated in the same way for tax purposes – it can be considered strange that only UCITS funds and special funds, and not investment enterprises, were made tax-exempt. However, this can be explained by that the new legislation had its basis in changes to the UCITS Directive that made it possible for Swedish UCITS funds to merge with foreign UCITS funds without any negative tax consequences.[91] The concern was that if Sweden continued to tax UCITS funds, while UCITS funds abroad were tax-exempt and could capitalise their profits in many cases, Swedish funds would start to merge with foreign funds, resulting in tax base erosion.[92] For this reason,

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[87] Chapter 39, sec 14 of the ITA

[88] Chapter 39, sec 14 of the ITA and Government Bill 1989/90:110 p 565.

[89] Gunne (n 29) p 778–779. See also, as an example, how the investment enterprise Investment AB Öresund "avoids" corporation tax through the payment of dividends in their annual report, 'Investment AB Öresund Årsredovisning 2018' p 13.

[90] Government Bill 2011/12:1 p 401.

[91] Government Bill 2011/12:1 p 401.

[92] Government Bill 2011/12:1 p 401.

the taxation of UCITS funds and special funds was moved from fund level to unitholder level, as will be explained in more detail below.[93]

Since the UCITS Directive only applies to UCITS funds and not to special funds, it could be considered peculiar that special funds were also made tax-exempt in 2012, since there was no similar "capital flight danger" for these funds. However, according to the Government, it was objectively justified to treat both special funds and UCITS funds the same for income tax purposes. To treat the two fund types differently would, according to the Government, risk distorting economic decisions regarding the choice of portfolio content, as well as make the tax rules unnecessarily complex.[94]

In relation to the current tax rules on investment funds, the following can be said. As stated above, Swedish UCITS funds and special funds are not legal persons. Nevertheless, the ITA stipulates that UCITS funds and special funds should be treated as legal persons, and consequently be considered as taxable entities, for income tax purposes.[95] This provision was inserted since the Government considered that a lack of such a provision could lead to that the unitholders of the funds were made liable to tax on the funds' income.[96]

Even if the funds are thus taxable entities, they are exempt from income tax.[97] In this respect, the taxation of UCITS funds and special funds has been replaced by a notional tax on unlimitedly taxable unitholders of these funds. Such unitholders are now required to enter an imputed income on their tax returns, consisting of 0,4 per cent of the value of their units at the beginning of each fiscal year ("lump sum taxation"), which is then taxed at the normal capital income tax

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93 Government Bill 2011/12:1 p 404.
94 Government Bill 2011/12:1 p 401.
95 Chapter 2, sec 3, subs 2 of the ITA.
96 Government Bill 2011/12:1 p 401.
97 Chapter 6, sec 5 of the ITA.

rate.[98] Such a tax is levied on unitholders in Swedish UCITS funds and special funds, as well as on unitholders in foreign investment funds that are equivalent to these fund types, since the Government considered that there should be tax neutrality between investments in foreign and domestic funds. [99]

In the Government Bill implementing the new tax system for investment funds, it was discussed whether it was at all necessary to add this additional tax on unitholders when making UCITS funds and special funds tax exempt. This question arose since UCITS funds and special funds were already, in principle, tax exempt before the new legislation was enacted if they distributed all their taxable profits to their unitholders.[100]

Nevertheless, it was stated that if no new rules on unitholder taxation were enacted, indirect investment through investment funds would become more beneficial than direct investment.[101] The reasoning runs as follows. When investment funds were made tax exempt, there would be no incentive for these funds to distribute dividends to the shareholders.[102] This would defer taxation at unitholder level and subject indirect investment to a lower effective tax rate than direct investment.[103] It is therefore possible to argue that the current lump sum taxation on unitholder level should rather be treated as a compensation for the previous taxation of dividends at unitholder level than as a compensation for the previous (non-)taxation at fund level.[104]

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[98] Chapter 42, secs 43–44, and Chapter 65, secs 7 and 10 of the ITA. See also Government Bill 2011/12:1 p 408. Such unitholders are of course also taxed on capital gains and dividends distributed from the funds.

[99] Chapter 42, secs 43–44 of the ITA do not specify that the provisions only apply to Swedish investment funds and from Chapter 2, sec 2 of the ITA it follows that the provisions in the ITA apply to both Swedish and foreign entities if not otherwise stated. See also Government Bill 2011/12:1 p 408 where it is stated that the new lump sum taxation applies both to foreign and domestic funds.

[100] Government Bill 2012/13:155 p 403.

[101] Government Bill 2012/13:155 p 403.

[102] Government Bill 2012/13:155 p 403.

[103] Government Bill 2012/13:155 p 403.

[104] See Dufwa, 'Utländska investeringsfonder, svensk kupongskatt och EU-rätt'. In: *Reglering och beskattning av investeringsfonder,* 2012 p 70–71 for similar reasoning.

3.4 Taxation of Swedish Alternative Investment Funds

There are no special tax rules for alternative investment funds, but instead the taxation of such funds follows the specific legal form of the alternative investment fund in question.[105] In the Government Bill implementing the Swedish AIFM Act, it is stated that it is not possible to create special tax rules for alternative investment funds due to the wide variety of categories and legal forms of such funds.[106] In this context, it was considered enough that specific rules existed for special funds, and for the remaining fund types normal tax rules would apply.[107]

Nevertheless, even if no mention of this was made in the Government Bill, it is possible that public alternative investment funds with legal personality, that have been admitted to trading on a regulated market, could fulfil the requirements necessary to be treated as fiscal investment enterprises.[108] However, it should be pointed out that before the Swedish AIFM Act came into force, the FSA indicated, in response to questions from some fiscal investment enterprises, that they did not have to apply for authorisation as internal managers of alternative investment funds under the Swedish AIFM Act. This was due to that they did not fulfil the alternative investment fund requirement of having a defined investment policy.[109]

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[105] Government Bill 2012/13:155 p 387.

[106] Government Bill 2012/13:155 p 391. Here, reference is expressly made to funds that are closed-ended, are not open for redemption at least once a year, do not apply the risk diversification principle and funds that invest in other assets than transferable securities.

[107] Government Bill 2012/13:155 p 391.

[108] Compare section 3.1 above.

[109] This was the case for Svolder AB as well as Investment AB Öresund. That Svolder AB is taxed as an investment enterprise follows from its annual report, 'Svolder AB Årsredovisning 2017/2018', p 70 and that Investment AB Öresund is taxed as an investment enterprise follows from its annual report (n 89) p 13. See also the FSA, 'Fråga om eventuell tillståndsplikt enligt LAIF' Dnr 14-1253 and the FSA, 'Fråga om eventuell tillståndsplikt enligt LAIF' Dnr 14-3178 where it was stated that these fiscal investment enterprises were not to be regarded as alternative investment funds. These files were obtained by the author at request from the FSA.

3.5 Withholding Tax, Foreign Investment Funds and Foreign Investment Enterprises

When Swedish UCITS funds and special funds were made tax-exempt, an exception from withholding tax on dividends was also inserted into the WTA. This provision was inserted since the Government considered that there were "indications" of that levying a withholding tax on dividends to foreign investment funds, while at the same time exempting their Swedish counterparts from income tax on dividends, would be contrary to EU law and especially the free movement of capital (Article 63 TFEU).[110]

The current withholding tax regime for foreign investment funds is structured in the following way. A 30 per cent withholding tax is levied on all outbound dividends from Swedish companies to foreign shareholders as a main rule.[111] However, an exception exists for "foreign UCITS funds" and "foreign special funds".[112] The exception only applies if the fund is established within the European Economic Area (EEA) or in a state with which Sweden has either concluded a general tax treaty that includes a provision on information exchange or a tax treaty that only deals with exchange of information.[113]

For the definition of foreign UCITS fund, reference is made in the WTA to a provision in the Swedish UCITS Act.[114] According to this provision, a foreign UCITS fund is a fund that satisfies the requirements of having as its sole object the collective investment in transferable securities or in other liquid financial assets through capital raised from the public, of allowing redemption or repurchasing of

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[110] Government Bill 2011/12:1 p 409.
[111] Secs 1, 4 and 5 of the WTA.
[112] Sec 4, subs 9 of the WTA.
[113] Sec 4, subs 9 of the WTA. In this context, it can be said that even if Article 63 TFEU applies in relation to all countries, the exception was for control reasons limited to countries with which Sweden had entered a treaty on information exchange in tax matters, see Government Bill 2011/12:1 p 409. See more on Article 63 TFEU in Chapter 4 below. It can be noted that both the Sweden-US DTC (Article 26) and the Sweden-UK DTC (Article 24) includes a provision on information exchange.
[114] Chapter 1, sec 1, para 9 of the Swedish UCITS Act.

units at the request of unitholders, and of operating the principle of risk spreading.[115] No definition is provided for the concept of "foreign special fund".

Lastly, it should be said that no particular withholding tax exception exists for foreign companies that, apart from their nationality, satisfy the ITA requirements for investment enterprise status.

3.6 Interim Summary – With a Special Focus on the Taxation of Dividends

As a summary of this chapter, it can be noted that special tax rules for Swedish UCITS funds, special funds, and investment enterprises have been enacted due to that these entities are mere intermediaries for collective investment in transferable securities used by a large number of individual investors. In practice, the special rules all lead to that these CIVs are exempt from income tax, and that the taxation is instead rolled over on the unitholders or shareholders of the CIVs, creating tax neutrality between the treatment of direct and indirect investment. For the purposes of this paper, it is important to highlight that because of these special rules neither investment enterprises nor UCITS funds and special funds typically pay any income tax on dividends.

Moreover, according to the WTA, foreign equivalents to UCITS funds and special funds are not subject to withholding tax on dividends, but there are no special rules exempting dividends to foreign equivalents to fiscal investment enterprises from withholding tax. It is against this legal background – which is displayed in diagram 2 below – that the assessment of current Swedish case law's compatibility with EU law will be made.

[115] Chapter 1, sec 1, para 9 of the Swedish UCITS Act.

Diagram 2 – The Swedish tax system in relation to collective investment vehicles (CIVs)

Entity / **Taxation**	**Swedish UCITS funds and special funds**	**Swedish fiscal investment enterprises**	**"Foreign UCITS funds" and "Foreign special funds"**	**Foreign CIVs that do not qualify as "Foreign UCITS funds" or "Foreign special funds"**
Taxation at fund level	Tax-exempt	Subject to tax, but can avoid tax liability in practice	Tax-exempt	Subject to withholding tax on Swedish-sourced dividends
Taxation at unitholder level (refers to persons unlimitedly taxable in Sweden)	Taxed notionally on holdings and taxed on dividends and capital gains	Taxed on dividends received from the investment enterprise and on capital gains	Taxed notionally on holdings and taxed on dividends and capital gains	Taxed on dividends received from the investment fund and on capital gains

4. The US Mutual Fund and the UK OEIC

4.1 Introduction

The focus of the previous chapters has been to describe how Swedish CIVs are structured, regulated and taxed. In contrast, the focus of this chapter is to present how some foreign CIVs, namely the US mutual fund and the UK OEIC, are structured, regulated, and taxed in their countries of residence.

Both US mutual funds and UK OEICs are companies with variable share capital established in a company form recognized by the applicable national law. In this respect, it can be recalled that by variable share capital it is meant that the share capital of an investment company increases or decreases with subscriptions and redemptions of shares in the company without any need for a formal procedure.[116] As stated in section 1.4 above, this leads to that an investment company's capital is always equal to its net assets.[117]

4.2 The US Mutual Fund

The US mutual fund has been singled out for closer study mainly because of the importance of such funds. The US fund market has been recognised as the largest fund centre of the world and towards the end of 2017, the Investment Company Institute estimated that US-registered investment companies had assets under management amounting to more than 22 trillion USD worldwide.[118] For this reason, a large part of the case law discussed in this paper also concerns such funds.

In this context, "mutual fund" is just another name for an US-registered open-ended investment company that offers its shares publicly.[119] When it comes to the

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[116] Fort and Jost (n 27) p 48.
[117] Fort and Jost (n 27) p 48.
[118] Investment Company Institute, *Investment Company Factbook*, 2018 p 32–33. Compare SOU 2002:56 p 518 and Riassetto (n 24) p 12 where the importance of the US fund market is discussed.
[119] Rowland and Kim, 'USA'. In: *The International Comparative Legal Guide to Public Investment Funds*, 2018 p 126–129 and 132 and KPMG New York, 'United States - Investment Funds & Private

structure of US mutual funds, it can be mentioned that they typically employ a fund manager, which is normally set up as a separate legal entity.[120] There are requirements that the assets of the fund must be kept separately from the assets of the fund manager, and for this reason most mutual funds appoint a custodian.[121] Lastly, a mutual fund has a board of directors that is responsible for monitoring the activities of the fund.[122]

As to the regulation of the US mutual fund, it can be noted that they are subject to requirements regarding capital structure, eligible investments and risk diversification, as well as subject to the supervision of the US Securities and Exchange Commission.[123] In literature, it has been argued that the regulation of the mutual fund satisfies similar objectives as the UCITS Directive, in particular when it comes to transparency and protection of the end investor.[124] Nevertheless, in comparison with Swedish UCITS funds and special funds, the regulation of US mutual funds deviates in some respects. As an example, US mutual funds can invest in illiquid assets. However, investments in illiquid assets may not exceed 15 % of the net assets, and some mutual funds restrict the possibility to invest in such assets by adopting specific fund rules.[125]

For tax purposes, a mutual fund can elect to be taxed as a so-called "Regulated Investment Company" (RIC). In order to be treated as a RIC, a mutual fund must meet an annual "qualifying income test". This test entails that 50 % of the mutual

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Equity', *Topical Analyses IBFD*, last reviewed on the 1st of February 2017 sec 1.1.2.1.2. It can be noted that in the US, the term "investment company" is used for a large number of different company forms, such as partnerships, grantor trusts, and corporations. However, as far as the author can tell, the only Swedish case not dealing with a corporation is the recent Administrative Court of Appeal of Sundsvall judgment delivered on the 14th of May 2018 in case 630–632-14, which in part concerned a Delaware Statutory Trust. However, during most of the years assessed in the case (2006-2008) the fund formed part of a Maryland Corporation.

[120] KPMG New York (n 119) sec 1.2.1. See also SOU 2002:56 p 518.

[121] KPMG New York (n 119) sec 1.2.2.

[122] Rowland and Kim (n 119) p 128.

[123] Rowland and Kim (n 119) p 128–129.

[124] Dickson and O'Shea, 'Non-EU Funds Can Be Charged Withholding Taxes, ECJ Advocate General Says in Emerging Markets', *Tax Notes International*, 6(73) 2014 p 546.

[125] Rowland and Kim (n 119) p 129.

fund's assets must consist of cash and securities. Securities that are not US government securities or securities of other RICs must be limited to an amount not greater than 5 % of the value of the issuer's assets and to an amount not greater than 10 % of the issuer's voting securities.[126] Moreover, an investment company must distribute at least 90 % of its taxable income, as well as 90 % of its net exempt interest income (income from tax-exempt bonds) to be qualified as a RIC.[127] If a mutual fund satisfies these requirements it will not be subject to income tax, provided that it distributes the full amount of its income to its shareholders.[128] This is because a US mutual fund qualifying as a RIC is allowed to deduct dividends paid to its shareholders, just as a Swedish fiscal investment enterprise.[129]

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[126] Rowland and Kim (n 119) and Rienstra, 'United States - Corporate Taxation', *Country Analyses IBFD*, last reviewed on the 1st of January 2019 sec 11.6.3.1.2.
[127] Rienstra (n 126) sec 11.6.3.1.2.
[128] Rienstra (n 126) sec 11.6.3.1.1.
[129] Rienstra (n 126) sec 11.6.3.1.3. See section 3.2 regarding the taxation of the Swedish fiscal investment enterprise.

4.3 The UK OEIC

The main reason for focusing on the UK OEIC in this paper is that Brexit makes the situation of this investment company especially interesting. Today, a large part of UK OEICs fall within the scope of the UCITS Directive. However, when (and if) Brexit occurs, these OEICs will no longer be regulated by the UCITS Directive, as the directive only applies to investment companies established within the EU.[130]

In this context, it is interesting to note that the UK Government has declared that after Brexit, the UK intends to maintain fund legislation based on UCITS, with the purpose of enabling the UK asset management industry "to continue to provide their services underpinned by a globally-renowned regulatory framework that ensures high levels of investor safeguards".[131] It is therefore likely that OEICs that are currently covered by the UCITS Directive will in the future be regulated in a similar manner even if they – from an EU law perspective – will then be classified as non-EU alternative investment funds.[132] If the current approach used by the Swedish lower courts and the Swedish Tax Agency is still applied then, this will result in that OEICs will go from being exempt from withholding tax to being subject to withholding tax overnight, even if there are no major changes made to the regulation of such funds.[133] The focus of this paper will be on such OEICs, which, it can be assumed, will fulfil similar regulatory requirements as Swedish

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[130] Article 1(1) of the UCITS Directive. It can be noted that no mention is made of the UCITS Directive in the current Brexit agreement between the UK and the EU. However, if this agreement comes into effect there will be a transition period during which the UCITS Directive will still be applicable in the UK, see Articles 126 and 127 of 'Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community', *Official Journal of the European Union*, C 66 I, 19 February 2019. However, if there is a so-called "hard" Brexit, the UCITS Directive will immediately cease to be effective in the UK.

[131] HM Treasury, *The UK Investment Management Strategy II*, 2017 p 13.

[132] Commins, 'Brexit: Implications for the Asset Management Sector'. In: *The International Comparative Legal Guide to Public Investment Funds*, 2018 p 17.

[133] See the Swedish Tax Agency's Position Statement published on the 20th of March 2017 (n 9) where the current distinction between UCITS investment companies and other investment companies is visible – a withholding tax is to be levied on all dividends to investment companies, with the exception of UCITS investment companies.

UCITS funds and Swedish special funds post-Brexit. As such, when UK OEICs are discussed below, it is the UK OEIC post-Brexit that is being referred to.

As regards the structure of the OEIC, it is led by a board of directors. One of these directors must be an Authorised Corporate Director (ACD), which is tasked with managing the fund. The ACD is almost always a legal person and the relationship between the ACD and the OEIC is similar to the relationship between Swedish UCITS funds or Swedish special funds and their management companies.[134] The fund's assets are held by a depositary.[135] OEICs (both UCITS and non-UCITS) are supervised by the UK Financial Conduct Authority.[136]

Lastly, when it comes to the taxation of the OEIC, it is subject to corporation tax but is exempt from tax on capital gains and dividends.[137] The favourable tax treatment of the OEIC is dependent on it fulfilling a "genuine diversity of ownership" test.[138] The aim of this test is to make sure that investment funds directed towards a limited group should not be able to benefit from the generous tax regime.[139]

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[134] Dunn and Malna, 'United Kingdom'. In: *The International Comparative Legal Guide to Public Investment Funds*, 2018 p 121 and SOU 2016:45 p 225. Also see section 2.2 below regarding the regulation of Swedish UCITS funds and Swedish special funds.

[135] Dunn and Malna (n 134) p 121.

[136] Dunn and Malna (n 134) p 121.

[137] Bal, 'United Kingdom - Corporate Taxation', *Country Analyses IBFD*, last reviewed on the 1st of November 2018 sec 11.6.1.

[138] Spielman, 'United Kingdom - Investment Funds & Private Equity', *Topical Analyses IBFD*, last reviewed on the 2nd of July 2018 sec 4.1.1.1.1.

[139] Spielman (n 138) sec 4.1.1.1.1.

5. The Scope of the Free Movement of Capital in Relation to Third Countries

5.1 Introduction

The focus of the above chapters has been to lay out a legal framework that will be used as a basis for the analysis of EU law and its implications for the Swedish dividend withholding tax system. Conversely, the focus of this and the coming chapters will solely be on EU law, starting with an analysis of Article 63 TFEU and how it applies in relation to third countries.

Initially, it should be said that Article 63(1) TFEU stipulates that all restrictions on the movement of capital between Member States and between Member States and *third countries* shall be prohibited. In this respect, "movement of capital" has repeatedly been stated to cover direct investments in companies resulting in dividend payments.[140]

From Article 65(1)(a) TFEU and Article 65(3) TFEU it can be gathered that Member States retain the right to distinguish between taxpayers who are not in the same situation with regard to their place of residence or to the place where their capital is invested, as long as the rules applied are not a means of arbitrary discrimination or disguised restriction on the free movement of capital. According to the CJEU, these provisions should be understood as a mere codification of case law in the sense that less favourable treatment of a foreign entity is only compatible with EU law if it concerns situations that are not objectively comparable or can be justified by an "overriding reason in the public interest".[141]

[140] See e.g. *Aberdeen* (n 1) para 33, *Emerging Markets* (n 1) para 33 and *Fidelity Funds* (n 1) paras 35–36.

[141] See e.g. *Emerging Markets* (n 1) para 57 and Case C-342/10 *Commission v Finland* [2012] EU:C:2012:688 para 34. See also Smit (n 17) p 556–557. "Overriding reasons in the public interest" will be explained more in detail in Chapter 8 below.

The purpose of this chapter is only to analyse the scope of the free movement of capital in relation to third countries. The questions of less favourable treatment, comparability, and justification will be further discussed in Chapters 6-8.

5.2 The Relationship between the Freedom of Establishment and the Free Movement of Capital

In the CJEU cases dealing with outbound dividends and investment funds the Court has continuously either applied the freedom of establishment (Article 49 TFEU), the free movement of capital (Article 63 TFEU), or both.[142] In contrast to the free movement of capital, the freedom of establishment does not apply in relation to third countries.[143] For this reason, it is important to establish in what cases the applicability of the freedom of establishment precludes the applicability of the free movement of capital.

In an intra-EU context, the CJEU has stated that the applicable treaty freedom should be decided by applying a two-step approach. As a first step, the purpose of the legislation should be looked at. If the national legislation is only intended to apply to shareholdings which enable the holder to exert a definite influence over a company's decisions and to determine its activities, then the legislation at issue should be assessed under Article 49 TFEU. Conversely, if the national legislation in question exclusively applies to shareholdings acquired solely with the intent of making a financial investment (so-called portfolio investments), then the legislation must be assessed under Article 63 TFEU.[144]

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[142] Freedom of establishment was applied exclusively in *Aberdeen* (n 1) see paras 34–35. The free movement of capital was applied exclusively in Case C-194/06 *Orange European Smallcap Fund (OESF)* [2008] EU:C:2008:289 see para 21, Joined Cases C-338/11 to C-347/11 *Santander Asset Management SGIIC* (*Santander*) [2012] EU:C:2012:286 see para 13, *Emerging Markets* (n 1) see para 33 and *Fidelity Funds* (n 1) see paras 35–38 . Both the freedom of establishment and the free movement of capital were applied in *Commission v Belgium* (n 1) see para 35.

[143] Article 49 TFEU.

[144] Case C-35/11 *Test Claimants in the FII Group Litigation II* [2012] EU:C:2012:707 paras 90–92.

If the national legislation applies indiscriminately to all shareholdings, and it is not possible to assess the applicable treaty freedom based on the purpose of the legislation, then the second step must be applied. According to this step, the factual circumstances of the case must be observed to determine the relevant freedom.[145]

However, the Court has stated that in cases concerning third countries, the same two-step approach should not be applied. In such a situation, the Court has stated that it is enough to only apply the first step, and if it is concluded that the national legislation at issue only applies to portfolio investments or applies indiscriminately to all forms of investments, then the free movement of capital is applicable. Conversely, it is only in cases where a provision *solely* applies to substantial shareholdings that the free movement of capital cannot be applied in a third country context.[146]

When applied to the tax provisions applicable for Swedish intermediaries, as well as the exemption from withholding tax for foreign investment funds, it can be noted that they apply indiscriminately to all forms of investments. Therefore, it can be argued that the free movement of capital is applicable in all third country cases dealing with these provisions, no matter the size of the shareholdings in the factual circumstances of the case.

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[145] *Test Claimants in the FII Group Litigation II* (n 144) paras 93–94.
[146] *Test Claimants in the FII Group Litigation II* (n 144) para 99 and *Emerging Markets* (n 1) para 30.

5.3 The Standstill Clause

The free movement of capital is the only free movement article in the TFEU that applies to states that are not Member States of the EU. In the negotiations leading up to the implementation of the article, this *erga omnes* principle was a controversial point, which caused the Member States to insert an exception to it in the form of a so-called standstill clause.[147]

The standstill clause, which is enshrined in Article 64 TFEU, allows Member States to continue applying discriminatory measures on the free movement of capital in certain circumstances. First, the restriction in question must only affect third countries. Second, the restriction must concern either 1) direct investment, 2) establishment, 3) the provision of financial services, or 4) the admission of securities to capital markets. Third, the restriction must have existed on the 31st of December 1993.

In the author's view, it can be argued that the standstill clause is of limited importance in cases dealing with US mutual funds or UK OEICs and outbound dividends. The primary reason for this is that it is only in rare cases that the material criteria of the standstill clause would be fulfilled in such cases. In this context, the CJEU has stated that portfolio investments are not covered by the concept of "direct investment".[148] This is of relevance since it is quite unusual for open-ended investment companies (such as US mutual funds or UK OEICs) to hold participations that give them a definitive influence over a distributing company.[149] Thus, most of the investments made by US mutual funds and UK OEICs are portfolio investments, precluding the applicability of the standstill clause.[150]

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[147] Smit (n 17) p 390–391 and p 643–644.

[148] Case C-446/04 *Test Claimants in the FII Group Litigation* [2006] EU:C:2006:774 para 196.

[149] Genta, 'Dividends Received by Investment Funds: An EU Law Perspective – Part 1', *European Taxation*, Journals IBFD, 53(2/3) 2013 p 83. Compare Article 52 of the UCITS Directive, where portfolio restrictions for UCITS funds are stipulated. See also Dahlberg (n 35) p 70.

[150] See Dufwa (n 104) p 77–78. It can also be questioned whether the temporal criterion is fulfilled since Swedish investment funds were made tax-exempt in 2012, compare *Emerging Markets* (n 1) paras 48–53. See also Case C-190/12 *Emerging Markets Series of DFA Investment Trust Company*,

6. Swedish Case Law

6.1 Introduction

When analysing cases dealing with outbound dividends, the CJEU has continuously applied a three-step approach. According to this approach, the CJEU first investigates if a fundamental freedom article could be applicable on the case at hand. Second, the Court conducts a restriction test, where it is investigated whether a foreign entity is treated less favourably than a domestic entity in an objectively comparable situation. Third, the CJEU conducts a justification test, where it tests if there are any applicable justification grounds for the discriminatory treatment and, if that is the case, if the restriction is proportional in the light of those justification grounds.[151]

The purpose of this chapter is primarily to assess how the second step (the restriction test) has been conducted by Swedish courts in relation to withholding taxes on dividends paid to foreign investment companies. More specifically, the focus will be on how the comparability analysis has been conducted, since the shift that has occurred in assessing comparable situations is what makes the case law particularly interesting. In contrast, the justification test, and the justification grounds considered by the Swedish courts, will only be mentioned briefly. Moreover, the presentation will concentrate on the assessments made by the *Swedish* courts, and the CJEU judgments referenced to in the cases will instead be presented more in depth in Chapters 7-8 below. It can be noted that in all the cases presented, the free movement of capital (Article 63 TFEU) was applied.

Opinion of Advocate General (AG) Mengozzi [2013] EU:C:2013:710 para 78 where the AG discusses that it is not likely that "the provision of financial services" would become applicable in a withholding tax case dealing with investment funds.

[151] Berglund and Cejie, *Basics of International Taxation: From a Methodological Point of View,* 2018, p 101 and Johansson (n 17) p 19–20. Other authors have divided up the steps differently, see e.g. Cejie (n 22) p 265–266, Genta (n 149) p 82 and Dufwa (n 104) p 67–68, but the overall content of the assessment is still the same.

The chapter will be structured in the following way. First, a background will be provided showing how Swedish courts assessed the Swedish withholding tax regime's compatibility with EU law before the SAC's ruling in HFD 2016 ref 22 (sec. 6.2). Subsequently, the reasoning of the SAC in HFD 2016 ref 22 and the closely related case HFD 2018 ref 61 will be explained (sec. 6.3). Thereafter, it will be shown how HFD 2016 ref 22 has led to a shift in the how the comparability analysis is conducted in withholding tax cases, with a special focus on the judgments of the National Board and the Court of Appeal discussed in the Introduction to the paper (sec. 6.3). The findings of the chapter will be summarised in a final section (sec. 6.4).

6.2 Case Law on the Swedish Withholding Tax Regime Before HFD 2016 ref 22

6.2.1 *Introduction*

The case law discussed in this section concerns the Swedish treatment of foreign investment companies in withholding tax situations under the legislation that existed pre-2012.[152] Here, it can be recalled that according to the legislation that existed before 2012, Swedish UCITS funds and special funds were subject to the same tax regime that is now applicable for Swedish fiscal investment enterprises. In other words, dividends paid by these funds were deductible, which often resulted in that no income tax on dividends was paid by these entities. At the same time, there was no exception from withholding tax on dividends for foreign investment funds.[153]

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[152] The Administrative Court of Appeal of Sundsvall judgments delivered on the 15th of February 2012 in cases 27-10, 693-10, 964-10, 980-10, 981-10, 1755-10, 1756-10, 2570-10, 2677-10 and 2683–2687-10. Also see the Administrative Court of Appeal of Sundsvall judgments delivered on the 15th of December 2014 in cases 862-13, 863–868-13, the judgments delivered on the 18th of December 2014 in case 38-14, the judgment delivered on the 27th of May 2015 in cases 880–884-13, 885–889-13, 894–895-13 and 896–900-13 and the judgment delivered on the 15th of June 2015 in case 665–669-14.

[153] See section 3.2 above.

The cases delivered before HFD 2016 ref 22 concern, inter alia, UK OEICs covered by the UCITS Directive, as well as US mutual funds with tax status as RICs.[154] In this section, focus will primarily be on the US mutual fund cases. Nevertheless, it can be noted that in the cases dealing with the UCITS OEICs, the Court of Appeal stated that the withholding tax levied on dividends to the foreign investment companies was contrary to EU law, without any in-depth comparability analysis. In the author's view, this can probably be explained by that the SAC had previously ruled, in a case dealing with the taxation of the investors of a UCITS investment company, that foreign UCITS funds are generally in objectively comparable situations with Swedish UCITS funds.[155]

6.2.2 *The US Mutual Fund Cases*

In this section, the US mutual fund cases will be referred to together as similar reasoning is applied in all the cases, with very few deviations. In these cases, the non-EU investment companies argued that they were treated less favourably than Swedish UCITS funds or special funds due to that the latter could avoid paying income tax on dividends in practice if they distributed their profits to their unitholders. The Court of Appeal agreed with the mutual funds that they were treated less favourably, since the withholding taxes levied on dividends discouraged them to invest in Swedish companies. The less favourable treatment could not be neutralised through the application of the Sweden-US DTC, since the US mutual funds did not pay any income tax in the US and could consequently not make use of any foreign tax credit.

When it comes to the comparability analysis, the Court of Appeal stated that the UCITS Directive should be used as a starting point and that it must be examined to what extent the regulation of the US mutual fund deviates from the provisions

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[154] The Administrative Court of Appeal of Sundsvall judgments delivered on the 15th of February 2012 concern SICAVs and OEICs. See cases 27-10 (SICAV), 693-10 (SICAV), 964-10 (SICAV), 980-10 (SICAV), 981-10 (OEIC), 1755-10 (OEIC), 1756-10 (OEIC), 2570-10 (SICAV), 2677-10 (OEIC) and 2683–2687-10 (OEIC). The rest of the cases mentioned in note 152 concern US RICs.

[155] RÅ 2006 ref 38.

in the Directive. Nevertheless, the Court stated that it should not be required that the regulatory framework of a US mutual fund is identical to the regulatory framework provided for by the UCITS Directive, with reference to the CJEU case *Emerging Markets.*[156] Moreover, the Court stated that the difference in legal form could not by itself lead to that the entities were considered non-comparable, since this would be contrary to EU law. The Court then concluded that there were enough similarities between how the US funds were structured and regulated and how favourably taxed Swedish investment funds were structured and regulated for them to be comparable.

The Court then added, once again with reference to *Emerging Markets,* that comparability should only be assessed based on the distinguishing criteria established in Swedish law for granting the tax exemption. Since the difference in treatment depended primarily on the residence of the investment fund in question (since only *Swedish* investment funds could be subject to the favourable tax treatment), and not on any regulatory requirements, the importance of the UCITS Directive for the comparability analysis was therefore in any case restricted.

The justification grounds considered by the Court were the need to safeguard the effectiveness of fiscal supervision, the need to preserve the coherence of the tax system, and the need to uphold a balanced allocation of taxing rights. All of these justification grounds were rejected by the Court with reference to *Emerging Markets.*

[156] *Emerging Markets* (n 1) para 67. This case will be discussed at length in sections 7.4.3 and 7.4.5 below.

6.3 HFD 2016 ref 22 and HFD 2018 ref 61

Before HFD 2016 ref 22, the Court of Appeal thus held that it was possible for non-EU investment companies to be in comparable situations with favourably taxed Swedish investment funds, as long as the regulation and structure of the former were similar to the regulation and structure of the latter.

When the new legislation came into force in 2012, it was assumed by the Swedish Tax Agency that the comparability analysis would be conducted in a similar manner when it came to determining the scope of the exception from withholding tax in the WTA.[157] For investment companies not covered by the UCITS Directive, an overall assessment should therefore be made regarding their regulation and structure to see if they were covered by the exception.

Nevertheless, as we shall see below, this approach – both in relation to the pre-2012 legislation and the new legislation – has been overturned as a result of the SAC's ruling in HFD 2016 ref 22. This case concerned the question of whether the value of the units in a non-UCITS Luxemburg SICAV (an investment company which has served as a model for the UK OEIC[158]) that fulfilled similar regulatory requirements as a Swedish special fund should be subject to a notional tax in the hands of unlimitedly taxable unitholders in Sweden. As stated in section 3.3 above, the value of units in Swedish UCITS funds and special funds, as well as in foreign equivalents to these funds, are subject to lump sum taxation every year at unitholder level.

The SAC ruled that non-UCITS foreign investment companies could not be considered equivalent to Swedish tax-exempt investment funds, and that the value of units in such funds should consequently not be subject to lump sum taxation, since the former were legal persons. This was motivated by that no special rules had been enacted for alternative investment funds, which are the only Swedish

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[157] The Swedish Tax Agency's Position Statement published on the 23rd of May 2012 (n 9).
[158] SOU 2016:45 p 277.

funds capable of assuming legal personality, and that the special Swedish tax rules had therefore “been enacted to deal with the fact that the funds in question are not legal persons”. No reference was made in the case to EU law.

The SAC has also subsequently repeated this view in HFD 2018 ref 61. In this case, which dealt with the tax consequences of a merger for the unitholders to a non-UCITS Luxemburg SICAV, the SAC stated that the SICAV could not be in a comparable situation with a Swedish special fund due to the difference in legal form. Moreover, this conclusion was deemed compatible with EU law since Swedish alternative investment funds with status as legal persons were not subject to favourable tax rules. The difference in treatment was therefore not based on residence, but on legal form, making the situations of the foreign investment company non-comparable to that of a Swedish contractual fund.

In the cases below, it will be shown how this reasoning of the SAC, in cases dealing with the members of investment funds, has spilled over on withholding tax cases.

6.4 Case Law on the Swedish Withholding Tax Regime After HFD 2016 ref 22

6.4.1 *The Court of Appeal Case 630–632-14*

In this case[159], which was delivered prior to HFD 2018 ref 61 and which has now been appealed successfully to the SAC, the question was whether it was compatible with EU law to levy a withholding tax on dividends to a US mutual fund with tax status as a RIC. It can be noted that this case concerned the years 2006-2008, that is before the 2012 legislative changes were made.

The Court of Appeal tested whether the US mutual fund could be compared to either a Swedish UCITS fund, a Swedish special fund, or to a Swedish fiscal investment enterprise. First, the Court referenced to *Emerging Markets* and stated that it could not be required that the US mutual fund was identical to a Swedish favourably taxed investment fund for objectively comparable situations to arise. Nevertheless, the Court stated that a requirement that the regulation of the foreign investment company should not deviate "too much" from the civil law regulation of Swedish investment funds was not the same as requiring perfect identity. For this reason, a legal form requirement was considered compatible with EU law, even when taking the CJEU *Aberdeen* case*,* which had been invoked by the US mutual fund, into account.[160] Here, the Court stated that in *Aberdeen,* the CJEU had not answered the question of whether a contractual fund could be compared to an investment company, but only the question of whether an investment company could be compared to a company having fixed share capital. Therefore, the Court of Appeal did not consider the *Aberdeen* case relevant in the case at hand.

Second, as regards the comparability with the fiscal investment enterprise, the Court stated that the US mutual fund had not shown that it fulfilled the ITA

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[159] The Administrative Court of Appeal of Sundsvall judgment delivered on the 14th of May 2018 in case 630–632-14.

[160] The *Aberdeen* case will be discussed at length in section 7.3 below.

requirement of almost exclusively investing in securities. For this reason, the Court of Appeal stated that objectively comparable situations did not arise.

6.4.2 *The National Board Case 4-17 D*

This case[161] – which was also delivered prior to HFD 2018 ref 61 – is the only case presented in this Chapter that deals with the legislation enacted in 2012 and, more specifically, the scope of the exception from withholding tax for foreign investment funds in the WTA. It did not concern a third country investment fund, but a non-UCITS Luxemburg SICAV, and the question was whether a withholding tax could be levied on dividends paid to it.

The majority of the National Board repeated the findings of the SAC in HFD 2016 ref 22 presented above and stated that the same assessment ought to be made in a withholding tax context. For this reason, the SICAV could not be equivalent to a Swedish special fund despite similarities in regulation, structure, and supervision. When it came to the question of whether this was compatible with EU law the National Board simply stated that the difference in legal form made the situations objectively different. Here, the National Board also stated that based on HFD 2016 ref 22 the unitholders of the SICAV would not be subjected to a notional tax on the value of their units, which was another factor that made the situation of the SICAV objectively different to the situation of a Swedish tax-exempt investment fund.

Three members of the National Board delivered a dissenting opinion. The minority stated that based on the CJEU case *Aberdeen* the legal form of the investment fund should not be treated as a decisive factor. Moreover, the minority considered that it should be possible to make a horizontal comparison between how a Luxemburg SICAV is treated and how a Luxemburg contractual fund is treated to find discriminatory treatment.[162] The minority considered, once again

[161] The National Board judgment delivered on the 30th of October 2017 in case 4-17/D.
[162] As stated in section 1.3 this part of the minority's ruling will not be addressed in the analysis below.

with reference to *Aberdeen,* that there were no applicable justification grounds for the discriminatory treatment in the case at hand.

6.5 Interim Summary and Questions that Arise

The focus of this chapter has been to describe how the comparability analysis has been conducted by the Swedish courts, both prior to HFD 2016 ref 22 and after. It has been shown that even if the case HFD 2016 ref 22 concerned the taxation of the investors of investment companies, the reasoning of the case has now "spilled over" on withholding tax cases. This applies both to cases dealing with the withholding tax system pre-2012 and cases dealing with the new withholding tax exception in the WTA. In this context, the Swedish Tax Agency has interpreted the closely related case HFD 2018 ref 61 as reinforcing the idea that the reasoning in HFD 2016 ref 22 can be applied generally, and hence also in withholding tax cases.[163]

It is interesting to note that neither *Emerging Markets* nor *Aberdeen* were discussed in the SAC cases, even if they were used as a basis for the argumentation in both the National Board and the Court of Appeal. In fact, the only EU case referenced to by the SAC is the case *Bouanich,* which does not concern the comparability of investment funds or even legal entities.[164] Moreover, it is interesting to note that the Court of Appeal based its argumentation on *Emerging Markets* both prior to HFD 2016 ref 22 and after HFD 2016 ref 22, with completely different results. Additionally, both the National Board minority and the Court of Appeal referred to the *Aberdeen* case with different outcomes.

The cases raise several questions that will be attempted to be answered in the following chapters. When it comes to comparability, the main question that arises

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[163] See the Swedish Tax Agency's Case Commentary (n 9).

[164] Case C-375/12 *Bouanich* [2014] EU:C:2014:138. This case was referenced to in HFD 2018 ref 61, while no references to EU law were made in HFD 2016 ref 22. In the case, which concerns a natural person, the CJEU held that the situations were comparable in two short paragraphs, and no in-depth analysis of the comparability issue was made, see paras 47–48.

is (1) if the current focus on legal form is compatible with EU law. A closely related question is (2) what the CJEU has based its comparability analysis on in cases dealing with investment funds.

As regards justification, there are also two more questions to answer: (3) if there are any justification grounds that could render the levying of withholding tax acceptable if it is found that a non-EU investment company is in a comparable situation with a more favourably taxed Swedish entity and (4) if the levying of withholding tax is proportional in the light of the justification grounds considered.

7. The Restriction Test in CJEU Case Law

7.1 Introduction

The purpose of this Chapter is to describe how the restriction test has been conducted by the CJEU in cases dealing with outbound dividends and investment funds, and to apply the findings on the Swedish withholding tax regime. As stated in section 6.1, the restriction test consists of two parts: first, the question of whether a cross-border situation is treated *less favourably* than a domestic situation, and second, the question of whether a cross-border situation is *objectively comparable* to a domestic situation.

One preliminary question that should be asked is whether a different restriction test should be made in a third country context in comparison with an intra-EU context. In this respect, the CJEU has held in several cases that a third country situation is not always comparable to an intra-EU situation, due to the degree of legal integration that exists between the Member States of the EU.[165] Nevertheless, in literature it has been pointed out that despite this statement, the restriction test has never been performed differently in a third country context by the CJEU.[166] This is also visible in the cases dealing with investment funds. For example, in *Santander,* which dealt with both investment funds covered by the UCITS Directive and US investment funds, the Court did not distinguish between the two fund groups when conducting the comparability analysis.[167]

For this reason, it will be assumed that the cases dealing with intra-EU situations discussed below are relevant in a third country context as well.

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[165] See e.g. *Test Claimants in the FII Group Litigation* (n 148) para 170 and *OESF* (n 142) para 89.

[166] See e.g. Smit (n 17) p 509, Bammens (n 17) p 525–526, Simander (n 17) p 168–172 and Lazarov, 'The Relevance of the Fundamental Freedoms for Direct Taxation'. In: *Introduction to European Tax Law on Direct Taxation*, 2018 p 83.

[167] *Santander* (n 142). Also see Viitala (n 43) p 154.

7.2 Less Favourable Treatment

Initially, it can be argued that it is quite clear from CJEU case law that less favourable treatment arises if a domestic entity does not pay any income tax on dividends – either due to a formal tax exemption or to de facto practice – while foreign entities are subject to a withholding tax on dividends.[168] For this reason, the focus of this chapter will primarily be on the comparability issue. Nevertheless, one aspect of the "less favourable treatment" issue ought to be discussed more in detail.

The aspect that should be discussed more in detail is that in none of the CJEU cases on CIVs looked at it has been possible to neutralise the less favourable treatment through the application of a tax treaty.[169] This is because in all the cases, the applicable tax treaty did not preclude the levying of tax on dividends in the source state and the tax levied could not either be set off in full in the residence state, due to that the fund assessed only paid a limited (if any) amount of tax there (as was the case in the initial US mutual fund cases delivered by the Court of Appeal).[170] When applied to UK OEICs and US mutual funds it is, in the author's view, therefore not likely that any less favourable treatment of them can be neutralised through the application of a tax treaty. This is because both these fund types only pay a restricted (if any) amount of tax in their residence states and the applicable DTCs both allow for the source taxation of dividends.[171]

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[168] See e.g. *Commission v Finland* (n 141) paras 32–33, *Santander* (n 142) paras 16–17 and *Aberdeen* (n 1) paras 40–41.

[169] See for a general discussion on this topic Cejie (n 22) p 285–287.

[170] See e.g. *Commission v Belgium* (n 1) paras 55–57 and *Commission v Finland* (n 141) para 63.

[171] See Chapter 4 above, Article 10 of the Sweden-US DTC and Article 10 of the Sweden-UK DTC. See also para 28 of the Commentary to Article 1 of the *OECD Model Tax Convention on Income and Capital* regarding that a US mutual fund or a UK OEIC are to be regarded as "beneficial owners" of a dividend payment.

7.3 The Importance of Legal Form

As stated in section 6.5, the main question raised from the recent developments in Swedish case law is if the current focus on legal form is compatible with EU law. In this regard, it is only in two of the cases examined that the issue of legal form has been addressed by the CJEU in the comparability analysis: *Aberdeen* and *Commission v Belgium.*[172] In this section, these cases will be discussed, followed by an assessment of their implications for the Swedish withholding tax system.

Aberdeen is the first CJEU case on outbound dividends dealing with an investment company.[173] The case concerned the payments of dividends to a non-UCITS Luxemburg SICAV (Nordic SICAV) from a wholly-owned Finnish company limited by shares (Alpha Oy).[174] The question was whether it was consistent with EU law to levy a withholding tax on dividends to Nordic SICAV, while a dividend paid from Alpha Oy to another Finnish company limited by shares or a Finnish investment fund would have been exempt from tax, either due to the Finnish rules on participation exemption or due to a special tax exemption for investment funds.[175] The Finnish law at the time did not allow for the establishment of companies with variable share capital, and consequently all Finnish funds were established in the contractual form.[176] Moreover, Finnish law did not allow tax-exempt investment funds to invest in real property, which Nordic SICAV did.[177] The Court found that the Finnish withholding tax regime amounted to an unjustified restriction to the freedom of establishment.[178]

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[172] *Aberdeen* (n 1) and *Commission v Belgium* (n 1).
[173] Viitala and Kujanpää (n 2) sec 2.2.
[174] *Aberdeen* (n 1) para 2.
[175] *Aberdeen* (n 1) para 39.
[176] Viitala (n 43) p 153–154.
[177] Viitala (n 43) p 153–154.
[178] *Aberdeen* (n 1) para 76. Freedom of establishment was the relevant freedom since Nordic SICAV owned all the shares in Alpha Oy and since the case concerned an intra-EU situation, compare section 5.2 above.

Much of the confusion surrounding the question of comparability of investment funds can be traced back to the *Aberdeen* case.[179] This is mainly due to that the CJEU only compared the SICAV to a Finnish company limited by shares and not to a Finnish investment fund. In this regard, the Court held that the circumstance that there was no company with a legal form identical to that of a SICAV in Finland was of no importance, since such a requirement would deprive the freedom of establishment of all effectiveness.[180] Consequently, a restriction was found already when comparing the SICAV to a Finnish company, and the CJEU held that it was not necessary to examine the comparability of the SICAV with a Finnish investment fund.[181]

That a comparison was first made to a Finnish company limited by shares, rather than to a Finnish investment fund, has been interpreted differently in tax law literature. According to Johanna Dufwa, the *Aberdeen* case suggests that a comparison with Swedish companies limited by shares should be made, rather than with Swedish contractual funds, in withholding tax cases dealing with investment companies.[182] This is then in line with the recent developments in Swedish case law discussed above.

In contrast, other scholars have interpreted the statement on legal form in *Aberdeen* more broadly, as connoting that legal form should as a rule not preclude comparability.[183] For example, Giampaolo Genta has argued that the approach in *Aberdeen* must be seen in the light of the specific circumstances of the case. This is because in the case at hand, it did not matter which entity was used as a comparator – the dividends would have been exempt from tax either way.[184] In Genta's view, *Aberdeen* should not be interpreted as meaning that a non-UCITS

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[179] Viitala (n 43) p 153–154.
[180] *Aberdeen* (n 1) para 50.
[181] *Aberdeen* (n 1) para 55.
[182] Dufwa (n 104) p 74.
[183] See e.g. O'Donnell and Molitor-March (n 11) p 141.
[184] Genta (n 2) p 144.

investment company cannot be in a comparable situation with a contractual fund, but rather that such an investment company can both be in a comparable situation with a company having fixed share capital *and* a contractual fund.[185] Genta's view – which largely builds on a purpose approach to comparability – will be returned to in section 7.4.5 below.

Thus, the *Aberdeen* case has led to diverging views in literature as to what the "right" comparator of an investment company is, and for this reason it is perhaps not strange that different interpretations of the case have been made by the minority of the National Board and the Court of Appeal.

The second case dealing with investment companies and legal form, *Commission v Belgium,* did not make the situation much clearer. This case concerned the previous Belgian withholding tax regime applicable for investment companies. Under this regime, a withholding tax was levied on dividends to both Belgian investment companies and to non-resident investment companies as a starting point.[186] However, investment companies resident in Belgium and non-resident investment companies with permanent establishments (PEs) in Belgium, could credit the withholding tax on dividends received by them against the corporation tax payable, and excess withholding tax could also be refunded.[187] The Court found that this regime was in conflict with both Article 63 TFEU and Article 49 TFEU.[188]

In the case, the Belgian Government argued that the non-resident investment companies should be compared to Belgian contractual funds (referred to in the case as "common funds") rather than to investment companies resident in Belgium. The reason for this was that Belgian contractual funds were not subject to corporation tax in Belgium, due to that they were treated as flow-through entities, and any

[185] Genta (n 2) p 146–147.
[186] *Commission v Belgium* (n 1) para 38.
[187] *Commission v Belgium* (n 1) para 38.
[188] *Commission v Belgium* (n 1) paras 83 and 87.

withholding tax levied on dividends to them therefore became final. This made the tax treatment of them identical to the treatment of non-resident investment companies without a PE in Belgium. However, the CJEU stated that contractual funds have a *different legal form* than non-resident investment companies, and that Belgium could not claim that the situation of non-resident investment companies should be compared to such funds on the sole basis that the tax legislation treated those two categories of taxpayers identically.[189]

At first glance, it appears as if *Commission v Belgium* supports the idea that investment companies should be compared to corporate entities rather than to contractual funds. However, it should be noted that the question in the case was whether non-resident investment companies should be compared to Belgian investment companies (Belgian legislation allows for investment companies having variable share capital, and such funds can also be covered by the UCITS Directive[190]) or contractual funds. For this reason, it is not strange that the Court referred to legal form and stated that it made more sense to compare the non-resident investment companies to resident investment companies rather than to resident contractual funds.

Moreover, the argumentation of the Belgian Government was rather weak in that the only argument brought forward for comparing non-resident investment companies with contractual funds was the similarity in tax treatment.[191] In this context, it can also be highlighted that the CJEU stated that comparability could not arise *solely* on that ground, indicating that perhaps there could be other factors that could make the situation of contractual funds comparable to those of investment companies, despite the difference in legal form. Consequently,

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[189] *Commission v Belgium* (n 1) para 59.

[190] Gruysmans, 'Belgium - Corporate Taxation', *Country Analyses IBFD*, last reviewed on the 1st of February 2019, sec 11.6.1.1.

[191] Compare Viitala (n 43) p 155.

Commission v Belgium does not shed much light on the question of what importance legal form has for the comparability analysis.

In the author's view, the only conclusion that can be drawn with certainty from the two cases discussed above is therefore that comparability cannot be denied solely on the ground that a certain legal entity does not exist in a jurisdiction (based on *Aberdeen*).[192] When applied to US mutual funds and UK OEICs, it can be argued that the minor difference in legal form between these entities and Swedish companies limited by shares should not stand in the way of comparability. In this context, it can be recalled that a Swedish company limited by shares is one of the entities capable of qualifying as a fiscal investment enterprise. However, additional criteria must also be fulfilled for this status to be granted.[193] For this reason, it is necessary to investigate if there are any other arguments in CJEU case law for or against seeing a non-EU investment company as comparable to this Swedish intermediary. The same goes for the question of whether a UK OEIC or a US mutual fund can be in a comparable situation with a Swedish UCITS fund or a Swedish special fund, since the cases discussed above do not provide a definite answer as to whether the difference in legal form precludes comparing these entities to each other.

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[192] Compare Viitala (n 43) p 153.
[193] See section 3.1 above.

7.4 The Purpose of the Legislation and Distinguishing Criteria

7.4.1 *Introduction*

As stated above, legal form has only been addressed by the CJEU in two of the withholding tax cases on CIVs. The question then arises as to what comparability factors have been considered in the other cases on investment funds reaching the CJEU. In this section, it will be argued that the case law developed by the CJEU indicates that two aspects should be treated as decisive: the purpose or aim of the legislation, and the distinguishing criteria established in the national legislation for receiving the favourable tax treatment.

The section will start by explaining how the purpose approach and the distinguishing criteria approach have been developed by using the cases *OESF, Commission v Belgium, Commission v Finland, Santander,* and *Emerging Markets* (sec. 7.4.2-7.4.3). Then, it will be shown how these two approaches have been refined and joined together in the cases *PMT* and *Fidelity Funds* (sec. 7.4.4). Lastly, a discussion will follow on the importance of these cases for the Swedish withholding tax regime (sec. 7.4.5).

7.4.2 *The Development of the Purpose Approach*

In almost all the cases dealing with outbound dividends coming before the CJEU, both concerning investment funds and other tax subjects, reference has initially been made to the purpose of the legislation in the comparability analysis. The Court has generally started by stating that when it comes to measures introduced by a Member State with the *purpose* of mitigating economic double taxation, or exempting profits from tax, non-resident shareholders are not necessarily in comparable situations with resident shareholders.[194] However, non-resident shareholders are generally comparable to resident shareholders if they are subject to a charge to tax on dividends in the source state, since the risk for economic

[194] See e.g. *Aberdeen* (n 1) para 42, *Commission v Belgium* (n 1) para 48 and *Emerging Markets* (n 1) para 58.

double taxation is then the same for non-resident shareholders as for resident shareholders.[195] It is solely through the exercise of taxing power by a Member State on non-residents that a risk of economic double taxation arises, contrary to the purpose of the legislation.[196] In other words, comparability has sometimes been established exclusively on the existence of a charge to tax, in light of the purpose with the legislation.[197]

In investment fund cases, these considerations are generally put forward by the CJEU when domestic funds are subject to a tax exemption that is not extended to foreign funds.[198] However, there are also examples of the CJEU assessing CIV taxation systems that do not make use of a simple tax exemption to achieve tax neutrality between direct and indirect investment. In these cases, the Court has often delved deeper into the purpose of introducing special tax rules for investment funds, either to support or deny comparability.[199]

The first case on investment funds that clearly addresses the specific purpose of creating tax neutrality between direct and indirect investment is the *OESF* case. This case dealt with the treatment of inbound dividends, but has nonetheless been recognised in literature as being relevant for outbound dividend investment fund cases as well.[200] The case concerned Orange European Smallcap Fund (OESF), a company with variable share capital resident in the Netherlands.

The Dutch tax legislation applicable for CIVs consisted of multiple layers, but for a discussion on purpose it is only relevant to point out the following aspects. According to Dutch law, a refund was granted to investment companies, such as OESF, for withholding taxes on dividends received from Dutch companies.

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[195] See e.g. *Aberdeen* (n 1) para 43, *Commission v Belgium* (n 1) para 49 and *Emerging Markets* (n 1) para 58.
[196] See e.g. *Aberdeen* (n 1) para 44, *Commission v Belgium* (n 1) para 50 and *Emerging Markets* (n 1) para 59.
[197] Tenore (n 45) p 147.
[198] See *Emerging Markets* (n 1) paras 47–51 and *Fidelity Funds* (n 1) paras 53–56.
[199] See Adema (n 39) p 17 regarding that the principle of transparency has been incorporated in almost all Member States in their taxation of UCITS.
[200] Genta (n 149) p 87 and Tenore (n 45) p 150–151.

Moreover, in relation to withholding taxes levied on dividends from foreign companies, a concession could be granted. However, this concession was restricted in two ways. First, a concession could only be granted in proportion to the amount of Dutch resident shareholders. Second, the concession was restricted to the amount that the investment company would have been able to credit based on a DTC with the source state of the dividend if the investment fund had been a natural person. In other words, the tax benefit (the concession) was subject to the criterion that a tax treaty existed between the Netherlands and the source state, granting a natural person a credit for withholding taxes levied in the latter.[201] The CJEU considered that the first criterion, but not the second criterion, was incompatible with Article 63 TFEU.[202]

In relation to the second criterion (the tax treaty criterion), the CJEU held that this was compatible with EU law having regard to the aim of the legislation. As stated above, the aim of the legislation was, just as the Swedish rules on CIVs, to create tax neutrality between the treatment of direct and indirect investment. In light of this aim, the CJEU held that it was justified to restrict the concession to situations in which the Netherlands had concluded a tax treaty with the other state, as it was only in those situations that a direct investor would have received a set-off for the tax paid on foreign dividends.[203] In contrast, the decision by a natural person to invest, through an intermediary, in companies situated in countries with which the Netherlands did not have a DTC did not involve the risk of losing a benefit which would have existed if the investment had been made directly.[204]

The next case that has been recognised as dealing with the specific purpose of investment fund tax regimes is the previously discussed case *Commission v*

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[201] *OESF* (n 142) paras 3–11

[202] *OESF* (n 142) paras 65 and 97.

[203] It can be noted that in the Netherlands there was no unilateral method for eliminating double taxation on passive income, see *OESF* (n 142) para 62.

[204] *OESF* (n 142) para 63.

Belgium.[205] This is because in this case, the CJEU briefly discussed whether the *activities* of non-resident investment companies could make them non-comparable to resident investment companies. In Viitala's view, such an assessment relates to the purpose of a CIV tax regime, since the basis for such a regime is that the specific activities of CIVs (the pooling of capital for collective investment to the benefit of investors) is what merits the introduction of specific rules.[206] Consequently, if a foreign entity performs other activities, it would not be contrary to the purpose of the legislation to deny that entity the favourable tax treatment.[207]

However, once again the Belgian Government relied on a rather weak argument, namely that the activities of resident investment companies differed from the activities of non-resident companies due to that they offered their shares to investors resident in different states.[208] For this reason, the Court refuted this argument by stating that it did not relate so much to any *intrinsic* differences between the activities conducted, but only to the fact that the activities were carried out in different Member States.[209]

The last case that should be addressed when it comes to the importance of the purpose behind a contested tax regime is *Commission v Finland.* Unlike the other cases discussed in this section, *Commission v Finland* concerned the treatment of pension funds instead of investment funds. Here, it can be noted that the case law concerning pension funds has been considered relevant for investment funds as well, since pension funds are also often subject to special dividend tax treatment due to the specific activities pursued by them.[210]

In Finland, both resident and non-resident pension funds were subject to tax on dividends received from the outset. However, Finnish pension funds could deduct

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[205] Viitala (n 43) p 155.
[206] Viitala (n 43) p 151–152 and p 155–156.
[207] Viitala (n 43) p 151–152.
[208] *Commission v Belgium* (n 1) para 58. Compare Viitala (n 43) p 155–156.
[209] *Commission v Belgium* (n 1) para 62.
[210] See e.g. Dickson and O'Shea (n 124), Hippert (n 45), Genta (n 149), and Viitala and Kujanpää (n 2).

amounts reserved by them to meet their obligations as regards pensions (*avsättningar för pensionsförpliktelser*), which often led to that they did not pay any income tax at all. In the Commission's view, this led to that Finnish pension funds were de facto exempt from income tax on dividends.[211] The CJEU agreed, and held that the Finnish system amounted to an unjustified restriction to Article 63 TFEU.[212]

One of the main questions of the case was whether the deduction for amounts reserved to meet pension obligations was an expense directly linked to an income generating activity in Finland. This question arose since the CJEU had previously held that non-residents and residents are typically only in comparable situations regarding deductions if the deduction is linked to such an expense.[213] The Finnish Government argued that a direct link was missing, since the deduction for amounts reserved to meet pension obligations related to the overall activity of the pension fund, and not any specific income generating activity.[214]

The Court refuted this argument and stated that the deductibility of reserves *was* linked to the specific income generating activity of procuring dividend income. First, this was supported by that the reserves were referred to in Finnish law as "expenses … incurred in order to acquire or maintain the income from economic activity". Second, this was the case since the deductibility of reserves had been inserted by the Finnish legislator to recognise the specific *purpose* of pension funds, which is to accumulate capital to procure capital income, particularly in the form of dividends, to meet future obligations under insurance contracts. The Court noted that this purpose could just as well have been taken into account by using another technique, such as a simple tax exemption.[215]

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[211] *Commission v Finland* (n 141) paras 25–26.
[212] *Commission v Finland* (n 141) para 54.
[213] *Commission v Finland* (n 141) para 37.
[214] *Commission v Finland* (n 141) paras 38–40.
[215] *Commission v Finland* (n 141) paras 41–42.

Then, the Court held that non-resident pension funds that pursued the same activity as Finnish funds also had the same specific *purpose*, leading to that they were in objectively comparable situations with Finnish funds.[216] In other words, the CJEU ruled that non-resident and resident pension funds were in objectively comparable situations as regards the deductibility of reserves, since they fulfilled the same purpose or activity. The basis for this was that the provisions allowing for deductibility of reserves, and consequently of dividend income, had been inserted to take this specific purpose or activity of pension funds (procuring capital income to meet future pension obligations) into account.

To sum up this section, it can be stated that the CJEU has relied on the purpose of the legislation in several cases concerning intermediaries either to deny comparability (as was the case in *OESF)* or to support comparability (as was the case in *Commission v Finland*). Below, it will be shown how this "purpose or activity test"[217] has been segmented through *PMT* and *Fidelity Funds.* However, first the distinguishing criteria approach will be presented.

7.4.3 *The Development of the Distinguishing Criteria Approach*

The distinguishing criteria approach was first introduced through the case *Santander. Santander* concerned the levying of withholding tax in France on dividends to non-resident UCITS funds and US investment funds.[218] UCITS resident in France were exempt from tax, whereas a withholding tax was levied on dividends to all non-resident CIVs.[219] The CJEU held that the legislation at issue was contrary to the free movement of capital.[220] For the sake of clarity, it can be noted that French legislation allows for the establishment of both contractual funds and investment companies.[221]

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[216] *Commission v Finland* (n 141) para 43.
[217] This term has been taken from Viitala (n 43) p 151.
[218] *Santander* (n 142) paras 2–6. It is unclear if the US investment funds are mutual funds or not; in the case the term "UCITS" is used for both the American and the European funds.
[219] *Santander* (n 142) paras 6–7.
[220] *Santander* (n 142) para 55.
[221] *Santander* (n 142) para 3.

In the case, the French Government argued that the question of whether the unitholders of the foreign CIVs were taxed in France on dividend income received should be relevant in the comparability analysis, since investment funds do not carry out investments on their own behalf but on the behalf of their unitholders.[222] However, the CJEU stated that only the *distinguishing criteria* established in the national legislation for being entitled to an exemption from tax on dividends should be taken into account in the comparability analysis.[223] In the present case, the sole criterion in the French legislation for being entitled to an exemption was the criterion of residency, since only investment funds resident in France could be exempt from tax on dividends.[224] Moreover, there was no link between the tax exemption for resident funds and the taxation on member level, since UCITS resident in France could capitalise the dividends received and still be tax-exempt on dividends.[225] For these reasons, the situations could only be compared at the level of the investment vehicle.[226]

The conclusion that the tax situation of the investors cannot be taken into account if their situation is not relevant, under national law, for granting the tax exemption in question has been reiterated by the Court in *Commission v Belgium* and *Emerging Markets*.[227] *Emerging Markets* is also relevant in another respect, since it does not only discuss distinguishing criteria in relation to the unitholders of the fund, but also in relation to the importance of the UCITS Directive.[228]

In this respect, it should first be said that *Emerging Markets* concerned the treatment of US investment funds under the Polish tax system. The Polish tax system was very similar to the French tax system in that Polish investment funds were exempt from tax on dividends, whereas a withholding tax was levied on

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[222] *Santander* (n 142) para 25.
[223] *Santander* (n 142) para 27.
[224] *Santander* (n 142) paras 28–29.
[225] *Santander* (n 142) para 30.
[226] *Santander* (n 142) para 39.
[227] *Commission v Belgium* (n 1) paras 65–67 and *Emerging Markets* (n 1) paras 61–63.
[228] *Emerging Markets* (n 1) paras 65–69.

dividends to non-resident investment funds.[229] The Court found that the Polish system was contrary to Article 63 TFEU.[230] It can be noted that Poland allows for the establishment of UCITS investment companies under its national law.[231]

In the case, the Polish Government argued that comparability should be denied on the basis that the US investment funds were not subject to the requirements laid down by the UCITS Directive, and that they were therefore in a different "legal and factual" situation to Polish-resident investment funds.[232] The CJEU first stated that non-compliance with the UCITS Directive cannot by itself be used as a basis for denying comparability, since such a requirement would deprive the free movement of capital of all practical effect in relation to third countries.[233] Then, instead of going deeper into any comparison of the US regulatory framework with the UCITS Directive, the Court repeated that only the criteria set out in the national legislation for granting a tax exemption could be taken into account in the comparability analysis. Consequently, since the Polish legislation only referred to the residency of the investment fund for granting the tax exemption, the Court held that

> a comparison of the regulatory framework governing funds established in a non-Member country and the uniform regulatory framework applied within the Union is of no relevance, in that such a comparison forms no part of the applicable legislation at issue in the main proceedings[234]

[229] This is a bit unclear from the judgment itself, since it is stated in it that under the current legislation both Polish investment funds and other EU UCITS funds could qualify for an exemption, see *Emerging Markets* (n 1) para 4. However, from the AG Opinion it follows that during the years that the main proceedings concerned (2005-2006) *only* Polish funds could qualify for an exemption from withholding tax, see Opinion of Advocate General Mengozzi (n 150) para 26.
[230] *Emerging Markets* (n 1) para 105.
[231] *Emerging Markets* (n 1) para 4.
[232] *Emerging Markets* (n 1) paras 65–66.
[233] *Emerging Markets* (n 1) para 67.
[234] *Emerging Markets* (n 1) para 68.

7.4.4 *The Joint Purpose and Distinguishing Criteria Approach*

The CJEU has accordingly referenced to both the purpose of the legislation and the distinguishing criteria laid down for receiving favourable tax treatment in cases dealing with intermediaries and dividend taxation. However, in some of the cases delivered, only one of these approaches have been used, and they have also been treated as separate approaches to comparability in literature.[235] In other words, even if both approaches have been used by the CJEU in its case law, it has been uncertain how they relate to one another and if they should be applied jointly or separately.

In the author's view, the most recent cases delivered by the CJEU on intermediaries and dividend taxation – *PMT* and *Fidelity Funds* – clarify that these two approaches to comparability should be applied jointly. As will be shown below, the distinguishing criteria approach is first used to pinpoint what factors are relevant for the comparability analysis. Then, the purpose approach is applied to investigate whether the use of these factors to distinguish between taxpayers is compatible with the aim of the legislation.

The *PMT* case, which is based on a reference for a preliminary ruling from the SAC, concerned dividends paid from Swedish companies to a Dutch pension fund (Pensioenfonds Metaal en Techniek (PMT)). These dividends were subject to a withholding tax on dividends, in line with the WTA. Conversely, Swedish pension funds were not subject to income tax on dividends, since they are taxed on all their income according to the Law on Yield Tax on Pensions (*Lag* (*SFS 1990:661) om avkastningsskatt på pensionsmedel*). The aim of the special taxation system for pension funds is to achieve neutrality between the taxation of different forms of pension savings, regardless of the economic climate surrounding various assets

[235] See e.g. *Santander* (n 142) which only discusses distinguishing criteria, *Commission v Finland* (n 141), which only discusses purpose, and Tenore (n 45) p 148–152.

and the pension products used.[236] The yield tax is intended to correspond to the normal taxation of all yields on capital.[237]

In *PMT* the CJEU started its comparability analysis by stating that:

> 48. It should be noted that the comparability of a cross-border situation with an internal situation must be examined having regard to the *aim* pursued by the national provisions at issue.
>
> 49. Moreover, only the relevant *distinguishing criteria* established by the legislation in question must be taken into account in determining whether the difference in treatment resulting from that legislation reflects an objectively different situation[238]

Then, the Court noted that the Swedish legislation set out a distinguishing criterion on the basis of residency, since only pension funds resident in Sweden could be subject to the yield tax.[239] Subsequently, the Court examined whether this distinguishing criterion was compatible with the objective, purpose and content of the legislation, and found that this was the case.[240] In short, the Court stated that the aim with the special Swedish yield tax (achieving neutrality between the treatment of different pension savings) could only be achieved if a fund was taxed on the whole of its assets. For this reason, it was consistent with the aim of the legislation to distinguish on the basis of residency, since Sweden could not tax non-resident pension funds on all their assets due to limitations arising from the application of DTCs.[241]

Fidelity Funds concerned the Danish withholding tax system in relation to UCITS funds. Under this system, both resident UCITS and non-resident UCITS were subject to a withholding tax on dividends from Danish companies from the outset.[242] However, Danish-resident UCITS could be exempt from withholding tax

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[236] Government Bill 1992/93:187 p 3 and p 157–158. See also *PMT* (n 48) para 12.
[237] Government Bill 1992/93:187 p 3 and p 157-158. See also *PMT* (n 48) paras 12 and 53.
[238] The paragraph numbers are taken from *PMT* (n 48) (emphasis added, and citation of case law omitted). The same paragraphs (with some small deviations) can be found in *Fidelity Funds* (n 1) paras 50–51.
[239] *PMT* (n 48) para 50.
[240] *PMT* (n 48) para 51.
[241] *PMT* (n 48) paras 54–62.
[242] *Fidelity Funds* (n 1) paras 4–5.

on dividends if they made a minimum distribution to their unitholders, alternatively calculated a minimum distribution, and withheld the tax payable by their investors on this actual or notional distribution.[243] In other words, the favourable treatment of UCITS in Denmark was dependent on two criteria: residency in Denmark, and the withholding of tax on a minimum distribution.

The *Fidelity Funds* case is not as clear-cut as the PMT case when it comes to the use of the joint purpose and distinguishing criteria approach. Nevertheless, the initial remarks of the comparability analysis were the same, namely that comparability must be assessed in the light of the aim sought, and the distinguishing criteria established, by the national legislation.[244] After making these statements, the CJEU recognised that the Danish legislation had two aims: to create tax neutrality between direct and indirect investment, by exempting dividends from taxation, and to ensure that dividends with a source in Denmark did not elude taxation in Denmark but were actually taxed at unitholder level, through the withholding of tax on the minimum distribution.[245] In relation to the first aim, the Court reiterated what has been stated above in relation to measures introduced to mitigate or eliminate double taxation, namely that resident and non-resident shareholders are generally in comparable situations in relation to such measures if they are both subject to a charge to tax.[246]

In relation to the second aim, the Court first recognised that Denmark could not subject non-resident UCITS to an obligation to withhold tax on a minimum distribution.[247] However, even if this was a criterion in the national legislation for receiving the favourable tax treatment, the Court did not think that it could be considered decisive having regard to “the aim, the subject and the content of the

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[243] *Fidelity Funds* (n 1) paras 9–13. It can be noted that the calculation option only existed after 2005, when new legislation was enacted, see para 13.
[244] *Fidelity Funds* (n 1) paras 50–51.
[245] *Fidelity Funds* (n 1) para 52.
[246] *Fidelity Funds* (n 1) paras 53–56.
[247] *Fidelity Funds* (n 1) paras 57–58.

legislation at issue in the main proceedings".[248] In the Court's view, the comparability analysis should focus on the "substantive conditions" laid down in national law for receiving the favourable tax treatment, which in this case was if Denmark *could tax* the unitholders' income or not, and not the actual *method of taxation* used.[249] In this context, the Court stated that a non-resident UCITS may have unitholders that are tax resident in Denmark, leading to that dividends distributed by them could also be taxed at unitholder level by Denmark.[250] The Court then added, rather cryptically, that even if Denmark could not tax non-resident unitholders on dividends received from non-resident UCITS, the absence of such a possibility was still "consistent with the logic of moving the level of taxation from the vehicle to the shareholder".[251]

It is interesting to note that in contrast to *Santander,* the Court discussed whether it was possible for Denmark to tax the unitholders of non-resident UCITS. The Court did not explain why the situation of the unitholders suddenly became important, but clues can be found in the Opinion delivered by the Advocate General. In the Advocate General's view, the Danish legislation at issue in *Fidelity Funds* differed from the French legislation in *Santander* since the Danish legislation established a link between the granting of the tax exemption to resident UCITS and the tax situation of the members.[252] In other words, one of the distinguishing criteria in the national legislation for being granted the tax exemption was that the unitholders of the UCITS should be taxed on a minimum distribution. For this reason, it is not strange that the situation of the unitholders was discussed by the CJEU.

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[248] *Fidelity Funds* (n 1) para 59.
[249] *Fidelity Funds* (n 1) para 59.
[250] *Fidelity Funds* (n 1) para 61.
[251] *Fidelity Funds* (n 1) para 62.
[252] Compare Case C-480/16 *Fidelity Funds and Others,* Opinion of Advocate General Mengozzi [2017] EU:C:2017:1015 para 50.

Moreover, it is of interest that the Court appears to suggest that even if Denmark could not tax non-resident unitholders on dividends received from non-resident UCITS, comparability should not be precluded since this was in any case "consistent with the logic of moving the level of taxation from the vehicle to the shareholder". At first glance, it appears as if the CJEU considers that the first aim (creating tax neutrality between direct and indirect investment) triumphs over the second aim (making sure that dividends did not evade taxation in Denmark). However, it can be noted that a withholding tax would have been levied on dividends paid to a non-resident investor investing *directly* in a Danish company.[253] It can therefore be argued that it *would* be consistent with the aim of creating neutrality between direct and indirect investment, as well as the aim of making sure that dividends did not evade taxation in Denmark, to levy a withholding tax on dividends from Danish companies to non-resident UCITS that only had non-resident shareholders.[254] Consequently, the reasoning of the CJEU in this part is somewhat hard to understand.

Nevertheless, it is still understandable that the CJEU held that the minimum distribution criterion should not be considered decisive in the comparability analysis. In the words of the Advocate General, this is because Denmark did "not consider the overall situation of UCITS members".[255] In particular, Denmark did not take into account that non-resident UCITS could also have unitholders resident in Denmark for tax purposes.[256] Thus, since the Danish legislation was not consistent with the taxation aim, it is not surprising that the importance of the minimum distribution criterion was limited, even if the CJEU's argumentation in relation to non-resident unitholders of non-resident UCITS is a bit unclear.

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[253] *Fidelity Funds* (n 1) paras 6–7.
[254] Compare *OESF* (n 142) para 63.
[255] Compare Opinion of Advocate General Mengozzi (n 252) para 51.
[256] Compare Opinion of Advocate General Mengozzi (n 252) paras 52–56.

As a conclusion, it is the author's opinion that *PMT* and *Fidelity Funds* show that the method currently applied by the CJEU in CIV dividend withholding tax cases consists of two steps. First, the Court investigates what the distinguishing criteria in the national legislation are for granting the favourable tax treatment. In *PMT,* the only distinguishing criterion found was residency. However, in *Fidelity Funds* it seems as if both the criterion of residency, and the criterion that the tax payable by unitholders should be withheld on a minimum distribution, were treated as distinguishing criteria.

Second, these distinguishing criteria are analysed in the light of the aim or aims with the legislation. In *PMT,* the residency criterion was considered compatible with the aim of achieving neutrality between the taxation of different forms of pension savings. In contrast, in *Fidelity Funds* the residency criterion was not consistent with the aim of the legislation, which was to achieve neutrality between direct and indirect investment by exempting profits from tax. Moreover, the CJEU considered that the second distinguishing criterion in *Fidelity Funds* – the withholding of tax on a minimum distribution – was inconsistent with the aim of making sure that dividends did not evade taxation in Denmark. Even if the reasoning of the Court in this part is not entirely clear, it can be argued that the primary reason for this was that the Danish legislation did not consider that there were other ways that dividends from non-resident UCITS could be taxed at unitholder level in Denmark.

Below, these two steps developed by the CJEU through its case law will be applied on the Swedish withholding tax regime.

7.4.5 *Implications for the Swedish Withholding Tax Regime*

In this section, the two steps (the distinguishing criteria approach and purpose approach) discussed above will first be applied to the rules governing Swedish UCITS funds and Swedish special funds, as well as foreign equivalents to these fund types. Both the currently applicable legislation and the pre-2012 legislation will be analysed, since cases concerning the latter are still reaching the Swedish courts (including the Court of Appeal case that has been successfully appealed to the SAC). Subsequently, the two steps will be applied on the legislation currently applicable for Swedish fiscal investment enterprises.

When applying the first step (the distinguishing criterion approach) to the currently applicable rules for investment funds it can be noted that the criteria for receiving the favourable tax treatment (the tax exemption) is either that a fund qualifies as a Swedish UCITS fund or special fund, alternatively that a fund qualifies as a "foreign UCITS fund" or a "foreign special fund". Since non-EU investment companies are only capable of qualifying as the latter, the result of the distinguishing criterion approach is that the concepts "foreign UCITS fund" and "foreign special fund" should form the basis of the comparability analysis.

In this regard, one point that can be stressed is that the Swedish legislation does not establish a link between the tax situation of the unitholders and the tax exemption at fund level. The exemption from tax is not made conditional on the taxation of the unitholders either under the WTA or the ITA; a Swedish UCITS fund or special fund is tax-exempt even if it only has limitedly taxable shareholders that are not subject lump sum taxation, and the same goes for foreign equivalents to these fund types under the WTA. For this reason, the argumentation of the National Board discussed in section 6.4.2 is flawed in stating that it is relevant in the comparability analysis whether unlimitedly taxable unitholders of a fund are subject to lump sum taxation or not.[257] Thus, even if it makes sense from a

[257] See section 6.4.2 above for the argumentation of the National Board.

domestic perspective to make the same assessment of a foreign fund in withholding tax cases as in cases dealing with the taxation of the investors, the distinguishing criterion approach appears to preclude such considerations in an EU law context.

In contrast, it can be argued that since the distinguishing criterion in Swedish legislation is not based on residency, but on whether the foreign fund type is equivalent to a Swedish UCITS fund or Swedish special fund, it *should* be possible to make a general comparison of the regulatory framework governing a foreign fund and the regulatory framework governing Swedish tax-exempt funds.[258] In this context, it can especially be recalled that the WTA even references to the Swedish UCITS Act and its definition of a "foreign UCITS fund". Consequently, in contrast to the *Emerging Markets* case, the UCITS Directive can be of relevance in the comparability analysis. Nevertheless, it must be kept in mind that not only "foreign UCITS funds" are exempt from tax in Sweden, but also "foreign special funds". For this reason, it would in the author's view be inconsistent with the distinguishing criterion approach to require full compliance with the provisions of the UCITS Directive.

Additionally, since the currently applicable Swedish withholding tax regime is based on an overall assessment of whether the foreign fund type is equivalent to a Swedish special fund or a Swedish UCITS fund, it cannot be considered wrong per se that the legal form of the foreign entity is discussed. This is because legal form requirements also form part of the regulatory framework governing Swedish UCITS funds and special funds.

However, moving on to the purpose approach, the question then arises as to whether treating legal form as decisive in the comparability analysis is compatible with the aim of the legislation. In this context, it seems to be the current position of the Swedish courts that the special rules for Swedish investment funds have

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[258] Compare Saïac and Rozant, 'Withholding Tax on Dividends Paid to Non-EU Investment Funds: Some Interesting Details', *European Taxation,* Journals IBFD, 54(10) 2014 p 469.

been inserted with the purpose of dealing with the fact that they are not legal persons.[259] However, in the author's view, there can be no doubt from reading the preparatory works that the general aim of the Swedish legislation is to achieve neutrality between direct and indirect investment, by exempting certain intermediaries well-suited for collective investment from tax. In contrast, the only provision in the ITA that has been introduced to deal with the fact that the Swedish fund types are not legal persons is the provision that states that Swedish UCITS funds and Swedish special funds *should be treated as legal persons*, and consequently as taxable entities.[260] It can be considered an anomaly that a provision that states that the fund types should be treated as legal persons is exactly what precludes comparing them to legal persons.[261]

Moreover, it can be argued that it is not because of legal form that no special rules have been enacted for alternative investment funds, but simply the fact that such funds are ill-suited and generally not used for collective investment by a large number of ("ordinary") investors. Here, it can also be recalled that alternative investment funds can be established in the contractual form as well. However, no special rules have been enacted for contractual alternative investment funds either, indicating that it is not the contractual legal form per se that merits the introduction of special rules.

In contrast, what makes Swedish UCITS funds and special funds stand out is that they both have as their sole object the collective investment in transferable securities or in other liquid financial assets, that they are as a rule open to the public, that they allow redemption or repurchasing of units and that they are subject to strict rules on investor protection. For this reason, it would be more consistent with the aim of the legislation to investigate if a foreign fund satisfies similar

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[259] See section 6.3 above.
[260] See section 3.3 above.
[261] Compare Arvidsson, 'A 12 Övriga juridiska personer' *Skattenytt,* 2017 p 319 where he discusses the outcome of HFD 2016 ref 22.

material criteria, as was done in the initial Swedish US mutual fund cases delivered, than to focus exclusively on formal criteria.[262] Moreover, in any case, both UK OEICs and US mutual funds are, just as Swedish contractual funds, established in a legal form especially well-suited for collective investment, since shares in such entities can be redeemed or repurchased without the need for a formal procedure.

Consequently, from the perspective that the "real" purpose of the Swedish legislation is to achieve neutrality between direct and indirect investment, by exempting certain entities well-suited for, and typically used by, a large number of individual investors from tax, it becomes difficult to maintain the legal form requirement. Returning to the *Aberdeen* case discussed above, which supports the idea that an investment company can be comparable to a Swedish company limited by shares, it is therefore possible to argue that a UK OEIC and a US mutual fund can be in a comparable situation with *both* a Swedish UCITS fund or Swedish special fund, *and* a Swedish company limited by shares.

As stated in section 7.3 above, this approach has been advocated by Genta. In Genta's view, the comparability analysis should ideally be conducted in two steps: first, investment companies should be compared to a domestic investment fund and, second, to a domestic company. This is because exempting investment companies from tax on dividends is both in line with the objectives of exempting investment funds from taxation, and in line with the objectives behind special tax rules applicable for corporate entities, such as participation exemption regimes.[263]

From Genta's perspective, the comparability of investment funds should focus on the material criteria in domestic law for granting the favourable tax treatment (such as being open to the public), and not on any formal requirements, such as legal form, since such requirements arise from the specific "domestic features" of

[262] See section 6.2.2 above. Compare Saïac and Rozant (n 258) p 469.
[263] Genta (n 2) p 146–147.

a country.[264] Genta argues that such an approach is supported by the fact that the CJEU refers to *objectively* comparable situations, and not to *subjectively* comparable situations in its case law.[265]

This latter thought is developed by António Calisto Pato and Priscilla Goes Seize. They state that it is acceptable that funds with different characteristics, such as open-ended and closed-ended funds, are not *objectively* comparable to one another. However, "making a distinction between investment funds that have the exact same characteristics just on the basis of legal form is performing a subjective comparison, which is for the authors methodologically wrong".[266]

In the author's view, the argumentation of the scholars above is convincing. This is because UK OEICs and US mutual funds are, in all other respects than legal form (for example when it comes to open-endedness and investor protection), more similar to a Swedish UCITS fund or special fund than to a Swedish company limited by shares. For this reason, it *does* make sense, as a first step, to compare these foreign fund types to such tax-exempt Swedish investment funds. Moreover, the subjectivity in the opposite approach, i.e. in treating legal form as decisive, can particularly be seen in how the UK OEIC will be treated after (a possible) Brexit, if the new approach to comparability is still being applied then. From the author's view, there can be no objective reason as to why this fund type should go from being comparable to a Swedish UCITS fund to being comparable to neither a Swedish UCITS fund nor a Swedish special fund when (and if) the UK leaves the EU, provided that the fund is still regulated in a similar fashion. In this respect, it can particularly be recalled that the comparability analysis has never been conducted differently by the CJEU in a third country context in comparison with an intra-EU context.[267]

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[264] Genta (n 2) p 146.
[265] Genta (n 2) p 146.
[266] Calisto Pato and Goes Seize, 'EC Law and Investment Funds: The Aberdeen Case', *EC Tax Review*, 3 2009 p 120.
[267] See section 7.1 above.

The same reasoning can be applied to the legislation that existed before 2012, with some deviations. To begin with, under the distinguishing criterion approach the main criterion for receiving the favourable tax treatment (deductibility of dividends distributed) was residency, since the favourable treatment only applied in relation to "*Swedish* investment funds" under the pre-2012 legislation. As such, the regulatory framework (including legal form requirements) surrounding Swedish UCITS and special funds should be of more limited importance under the pre-2012 legislation in contrast to the currently applicable legislation, having regard to *Emerging Markets*. Moreover, it should be clarified that similarly to the currently applicable legislation, the situation of the unitholders should not become relevant. This is because Swedish UCITS funds or special funds could deduct dividends distributed by them under the pre-2012 legislation no matter if the dividends were taxed at unitholder level or not.

When applying the purpose approach on the residency criterion, it would be easy to state that the purpose of the Swedish legislation pre-2012 was to mitigate economic double taxation, and that residents and non-residents are therefore in comparable situations under that legislation as long as they are both subject to a charge to tax. This view has also often been adopted by Swedish lower courts when assessing the legislation that existed before 2012.[268] However, this perspective neglects the fact that the pre-2012 favourable tax regime was based on a *deduction* provision and not an *exemption* provision.[269] As such, it follows from CJEU case law that the relevant question to ask is not whether a charge to tax exists, but whether the deduction concerns expenses directly linked to an income generating activity.[270]

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[268] The Administrative Court of Appeal of Sundsvall judgments delivered on the 15th of February 2012 in cases 27-10, 693-10, 964-10, 980-10, 981-10, 1755-10, 1756-10, 2570-10, 2677-10 and 2683–2687-10.

[269] Compare Lohela (n 36) p 49 where she criticizes this aspect of the Swedish case law.

[270] *Commission v Finland* (n 141) para 37.

In the author's view, it is therefore the CJEU's reasoning in *Commission v Finland* that should be applied on the case at hand. Admittedly, distributed dividends are not referred to in Swedish legislation as "expenses … incurred in order to acquire or maintain the income from economic activity". However, just as in the Finnish case, the possibility to deduct dividends has been inserted by the Swedish legislator to recognise the specific *purpose* of investment funds, which is to gather capital from a great number of unitholders to invest it to the benefit of those unitholders and procure capital income, particularly in the form of dividends. Moreover, just as in the Finnish case, this purpose could just as well have been considered by using another technique, such as a simple tax exemption. For this reason, it can be argued that the deductibility of dividends distributed is connected to the income generating activity of procuring dividends, and that non-resident investment companies that satisfy a similar purpose as Swedish UCITS funds or special funds are in objectively comparable situations as regards the deduction provision. Consequently, the residency criterion pre-2012 appears to be at odds with EU law, having regard to the purpose of the legislation.[271]

Nevertheless, even if it can be argued, under the purpose approach, that legal form should not preclude comparing a Swedish UCITS fund or special fund to a UK OEIC or US mutual fund, this conclusion is far from certain. In particular, it can be recalled that in *Aberdeen* the CJEU did not adopt the approach advocated above, of first comparing an investment company to a domestic investment fund and then to a domestic company. As stated above, it is Genta's opinion that this can probably be explained by the specific circumstances of the case. Nevertheless, the uncertainty surrounding this question makes it necessary to ascertain what

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[271] Compare *Commission v Finland* (n 141) paras 41–43. Also see *PMT* (n 48) paras 64–65, where comparability in relation to deductions is discussed. The choice has been made to only discuss *Commission v Finland* here since the legislation in this case relied solely on a distribution provision to achieve its purpose and since the purpose could alternatively have been achieved by using a simple tax exemption (similarly to the pre-2012 Swedish legislation applicable for investment funds), which was not the case in *PMT*.

would happen if a UK OEIC or a US mutual fund could only be compared to a corporate entity.

Here, it should be possible to find discrimination when comparing a UK OEIC or a US mutual fund to a Swedish company limited by shares (or an alternative investment fund established in this corporate form) qualifying as a Swedish fiscal investment enterprise. Admittedly, there are some differences between these entities, such as that UK OEICs and US mutual funds are open-ended CIVs, while Swedish fiscal investment enterprises are closed-ended CIVs. However, since only the distinguishing criteria laid down in the national legislation for granting the favourable tax treatment can be taken into account, this difference should not be of importance. Instead, the only criteria that should be assessed are the criteria 1) of being a Swedish company limited by shares or a Swedish cooperative 2) of having a great number of individual shareholders 3) of exclusively or almost exclusively managing securities and 4) of having risk diversification as a principal object by maintaining a diversified portfolio of securities.[272]

In relation to the first criterion, *Aberdeen* suggests that the small difference in legal form between a Swedish company limited by shares and a UK OEIC or US mutual fund should not preclude comparability. Moreover, for the same reasons as the ones stated above in relation to the pre-2012 legislation applicable for Swedish investment funds, it should not be necessary to fulfil the residency criterion since this criterion appears to be at odds with the purpose behind the legislation.

Regarding the three other criteria, it can be argued that they are, just as the minimum distribution criterion in *Fidelity Funds*¸ separable from the criterion of residency so that a separate assessment should be made of whether they are consistent with the purpose of the legislation. As stated in section 3.1 above, these criteria have probably been inserted to make sure that the favourable tax treatment of fiscal investment enterprises is only extended to those enterprises that are well-

[272] Chapter 39, sec 15 of the ITA.

suited, and used, for collective investment by a large number of individual investors.[273] As such, they appear to be compatible with the legislation's purpose.

In this respect, some US mutual funds may have difficulties fulfilling the criterion of almost exclusively investing in securities, since they can also invest in illiquid assets. However, as stated in section 4.2 above, the possibility to invest in such assets can be restricted through the adoption of specific fund rules, and it is also clear from the initial US mutual fund cases delivered by the Court of Appeal that such specific fund rules are often adopted.[274]

Nevertheless, it cannot be considered wrong that comparability with a Swedish fiscal investment enterprise was denied in the latest Court of Appeal judgment, when the foreign fund had not shown that this latter criterion was fulfilled. In this context, it appears as if the US mutual fund mainly presented evidence in support of that it was *taxed* in a similar fashion as a Swedish fiscal investment enterprise, and that evidence regarding its regulation was lacking. In the author's view, this is regretful and also odd in light of CJEU case law, since the CJEU has repeatedly held that the tax situation of a foreign CIV in its state of residence is of no importance in the assessment of comparable situations in dividend tax cases.[275]

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[273] This can be compared to the UK OEIC "genuine ownership test", see section 4.3 above.

[274] See e.g. the Administrative Court of Appeal judgments delivered on the 15th of December 2014 in case 862-13 and in cases 863–868-13, on the 18th of December 2014 in case 38-14 and on the 27th of May 2015 in cases 880–884-13. In the cases, such portfolio restrictions are referred to as "standard restrictions".

[275] See e.g. *Aberdeen* (n 1) para 52 and *Commission v Belgium* (n 1) paras 61–62. See also the Administrative Court of Falun's judgment delivered on the 2nd of December in case 667–680-12 (which later became case 630–632-14 in the Court of Appeal) where it is also stated that evidence is lacking regarding the regulation of the foreign fund.

7.5 Interim Conclusion

The purpose of this Chapter has been to describe how the restriction test has been conducted by the CJEU in cases dealing with outbound dividends and CIVs, and to apply the findings on the Swedish withholding tax regime.

In relation to the issue of *less favourable treatment*, it was first concluded that it is clear from CJEU case law that such treatment arises if foreign entities pay tax on dividends, while domestic entities do not. Additionally, in relation to UK OEICs and US mutual funds, it is difficult to neutralise any less favourable treatment of them under the applicable DTCs.

When it comes to the question of *objectively comparable situations*, the main conclusion of this Chapter is that it should be possible, under a joint distinguishing criterion and purpose approach, to compare a UK OEIC or a US mutual fund to a Swedish UCITS fund or special fund. This is because, in light of the purpose of the legislation, it makes more sense to focus on material criteria, rather than formal criteria, in the comparability analysis. This is also supported by that the CJEU refers to objectively comparable situations rather than to subjectively comparable situations in its case law. For this reason, the current Swedish lower court case law can be criticised since it mainly focuses on the distinguishing criteria laid down in the legislation at hand (including legal form requirements) and not on whether the focus on legal form is compatible with the actual purpose of the legislation.

However, it was also shown that there is no clear answer in CJEU case law as to what importance legal form has for the comparability analysis. For this reason, it was argued that it should alternatively be possible to compare a UK OEIC or a US mutual fund to a Swedish company limited by shares (or an alternative investment fund established in this corporate form) qualifying as a fiscal investment enterprise. Here, it should not be necessary for a UK OEIC or a US mutual fund, in light of *Aberdeen* and the purpose approach adopted by the CJEU in its case law, to fulfil the criterion of being a "Swedish company limited by shares". However, it should be necessary for the non-EU investment companies to fulfil the

other criteria that a Swedish fiscal investment enterprise must fulfil for comparability to be established. This is because the other criteria, such as almost exclusively investing in securities, can be considered compatible with the purpose of the legislation.

As a final conclusion of this Chapter, it can be said that while CJEU case law on dividends and investment funds is far from clear, there are indications that a UK OEIC or a US mutual fund can be in a *comparable situation* with either a Swedish tax-exempt investment fund or a Swedish company limited by shares qualifying as a fiscal investment enterprise. In any case, it is clear that a UK OEIC (post-Brexit) and a US mutual fund is treated *less favourably* under current Swedish lower court case law than any of the Swedish entities when it comes to the taxation of dividends. For this reason, it is necessary to investigate whether a restriction to the free movement of capital would be possible to justify.

8. The Justification Test in CJEU Case Law

8.1 Introduction

In this Chapter, it will be assessed how the justification test has been performed by the CJEU in cases dealing with outbound dividends and investment funds, and to discuss the implications of the case law for the Swedish withholding tax system. It can be recalled that the justification test consists of two parts, the question of whether any *justification ground is applicable* and the question of whether a restriction is *proportional* in the light of an applicable justification ground.[276]

In theory, it is possible to find justification grounds either in CJEU case law, known as "overriding reasons in the public interest", or in the TFEU. However, in the direct tax area, the explicit justification grounds in the TFEU have been considered irrelevant, and for this reason the CJEU typically only references to "overriding reasons in the public interest" in its case law on dividend taxation.[277]

The focus of this chapter will therefore only be on such "overriding reasons in the public interest". Moreover, the choice has been made to primarily focus on *one* such justification ground, namely the need to safeguard the coherence of the tax system. This choice has been made since this is the only justification ground that has been accepted by the Court in cases on dividends and investment funds, both dealing with intra-EU and third country situations.[278] In contrast, the grounds effectiveness of fiscal supervision[279], balanced allocation of taxing powers[280], the

[276] See section 6.1 above.
[277] Simander (n 17) p 181 and Lazarov (n 166) p 86. Compare section 5.1 above.
[278] *Fidelity Funds* (n 1) para 82.
[279] *OESF* (n 142) paras 91–92 and *Emerging Markets* (n 1) paras 76–88.
[280] *Santander* (n 142) para 48, *Commission v Belgium* (n 1) paras 76 and 79 and *Fidelity Funds* (n 1) paras 67–76.

need to prevent tax evasion[281], territoriality[282], and reduction of tax revenue[283] have systematically been rejected by the Court.

It can be noted that in contrast to the restriction test, the justification test is sometimes conducted differently in a third country context in comparison with an intra-EU context.[284] However, this is only true in relation to certain justification grounds, and the need to preserve the coherence of the tax system is not one of them.[285] Consequently, it will be assumed that the intra-EU cases presented below are of relevance in a third country context as well.

8.2 The Need to Safeguard the Coherence of the Tax System and Proportionality

The need to safeguard the coherence of the tax system has been addressed by the CJEU in almost all the withholding tax cases on dividends and intermediaries looked at. As such, it is clear from the Court's case law that for this ground to be accepted, a direct link must be established between the tax advantage concerned and the compensating of that advantage by a particular tax levy, with the direct nature of that link falling to be examined in the light of the objective pursued by the rules in question.[286] It can be noted that in previous case law this direct link had to exist for the *same* taxpayer, but that recent case law shows that the disadvantage and advantage can be found at *different* taxpayer levels, as long as there is a direct link between them.[287]

In all the cases looked at apart from one, this justification ground has been rejected by the CJEU due to the absence of such a direct link. For example, in

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[281] *Aberdeen* (n 1) paras 58 and 63–64.
[282] *Commission v Finland* (n 141) paras 46–47.
[283] *OESF* (n 142) para 95 and *Emerging Markets* (n 1) paras 102–103.
[284] Simander (n 17) p 263.
[285] *Emerging Markets* paras 90–92. Also see Simander (n 17) p 268 and the case law cited there.
[286] See e.g. *Emerging Markets* (n 1) para 92 and *Santander* (n 142) para 51.
[287] Genta (n 2) p 150 and Case C-493/09 *Commission v Portugal* [2011] EU:C:2011:635, *Santander* (n 142), and, most importantly, *Fidelity Funds* (n 1) where the Court accepted this justification ground.

Santander the CJEU held that this justification ground could not be relied on since the exemption from withholding tax for French UCITS was not made conditional upon redistribution and taxation of the dividends at unitholder level.[288] The same conclusion was reached in several other cases, including *Aberdeen* and *Emerging Markets*.[289]

However, in *Fidelity Funds* this justification ground was accepted by the Court. In this case, the CJEU stated that there was indeed a direct link between the tax advantage (the exemption from withholding tax) and the taxation of dividends in the hands of the members (through the withholding of tax payable by them on a minimum distribution).[290] Nevertheless, the Danish system was not considered *proportional* in the light of this justification ground. According to the Court, this was because a less restrictive measure would have been to allow non-resident investment funds to choose to be covered by the tax exemption, if they retained and paid a tax equivalent to the tax that Danish tax-exempt funds were required to retain.[291] This is of importance since Danish-resident investment funds could deduct certain losses and administrative expenses when calculating the minimum distribution.[292] Consequently, the tax withheld on the minimum distribution relating to dividends received would often be lower than the withholding tax that would otherwise have been retained at source by a Danish company.[293]

When applied to the Swedish withholding tax system, it can be noted that under the currently applicable system for Swedish UCITS funds and special funds, there is no direct link between the tax exemption and taxation at unitholder level. This is because Swedish UCITS funds and special funds can capitalise the dividend income received by them and still be entitled to the tax exemption. In other words,

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[288] *Santander* (n 142) para 52.
[289] *Emerging Markets* (n 1) para 93 and *Aberdeen* (n 1) para 73. See also *Commission v Portugal* (n 286) paras 38–39 and *Commission v Finland* (n 141) paras 48–52.
[290] *Fidelity Funds* (n 1) para 82.
[291] *Fidelity Funds* (n 1) para 84.
[292] *Fidelity Funds* (n 1) para 12.
[293] Opinion of Advocate General Mengozzi (n 252) para 58.

the tax advantage is not dependent on the redistribution and taxation of dividends at unitholder level. In this context, it can also be mentioned that the current lump sum taxation at unitholder level should not be enough to establish a direct link, since Swedish investment funds can qualify for the tax exemption even if they only have limitedly taxable unitholders that are not taxed notionally on the value of their units.[294]

However, when assessing the legislation applicable before 2012 for Swedish UCITS and special funds, as well as the legislation currently applicable for Swedish fiscal investment enterprises, the analysis becomes more complicated. This is because in this case, the favourable tax treatment (deduction of dividends distributed) *is* linked to the *redistribution* of dividends. Moreover, it can be noted that dividends distributed by Swedish investment funds and Swedish fiscal investment enterprises are as a rule either *taxed at unitholder level* under the WTA (for limitedly taxable unitholders) or under the ITA (for unlimitedly taxable unitholders).[295] Additionally, dividends distributed by Swedish intermediaries to unlimitedly taxable unitholders are usually subject to a preliminary tax deduction under the Tax Procedure Act (*Skatteförfarandelagen (SFS 2011:1244)*).[296]

Therefore, it can be argued that there *is* a direct link between the tax advantage (de facto exemption from tax) and the redistribution of proceeds and the immediate taxation of them at unitholder level (either through the WTA or ITA combined with the Tax Procedure Act). As such, it is possible to argue that the need to safeguard the coherence of the tax system could become applicable as a justification ground under the pre-2012 legislation for investment funds or the currently applicable legislation for fiscal investment enterprises. This conclusion

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[294] Compare Dufwa (n 104) p 77.

[295] Secs 1 and 4 of the WTA and Chapter 42, sec 1 of the ITA.

[296] Secs 1 and 4 of the WTA and Chapter 8, sec 4 and Chapter 10, sec 2 of the Tax Procedure Act. The preliminary tax deduction can be repaid if it is later shown that tax has been levied contrary to the provisions of the ITA, see Chapter 64, sec 2 of the Tax Procedure Act.

is then contrary to the conclusion reached by the Court of Appeal in the initial US mutual fund cases delivered.[297]

Nevertheless, two counter arguments to this conclusion may be presented. First, the Swedish legislation appears to differ from the Danish legislation in *Fidelity Funds* in that it does not explicitly state that withholding tax must be withheld on dividends for the intermediaries to qualify for the favourable tax treatment. Second, there is no guarantee that dividends distributed are actually taxed at unitholder level, since certain members of the Swedish intermediaries could be exempt from tax in their turn.

Nevertheless, in the author's view, it is at least possible to question the first counter argument. In relation to this argument, the recent developments in the pending case *Köln-Aktiefonds Deka* are of interest.[298] In this case, the Dutch Supreme Court (*Hoge Raad der Nederlanden*) initially asked the CJEU three questions on dividend taxation and investment funds. However, in light of the CJEU's judgment in *Fidelity Funds,* one of these questions was retracted.[299]

Through its retracted question, the Dutch Supreme Court asked the CJEU whether it was consistent with Article 63 TFEU to deny a non-resident investment fund a refund for withholding tax levied on dividends from Dutch companies, while such a refund could be granted to resident investment funds. The basis for the difference in treatment was that resident investment funds distributed the proceeds of their investments on an annual basis and withheld Dutch tax on this redistribution.[300] In this context, it is important to note that the Dutch legislation is similar to the Swedish legislation in that it does not explicitly state that tax must

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[297] See section 6.2.2 above.
[298] Case C-156/17 *Köln-Aktiefonds Deka* (pending).
[299] Offermanns, 'Netherlands; European Union - ECJ preliminary ruling: Aktienfonds Deka (Case C-156/17) – tax refund for non-resident investment fund – questions partially maintained', *News IBFD*, published on the 23rd of January 2019.
[300] 'Request for a preliminary ruling from the Hoge Raad der Nederlanden (Netherlands) lodged on 27 March 2017 — Köln-Aktienfonds Deka v Staatssecretaris van Financiën' *Official Journal of the European Union*, C 168, 29 May 2017.

be withheld at source for a domestic investment fund to receive a refund. Instead, it is only stated that a Dutch-resident investment fund must distribute its profits within eight months of the close of the financial year.[301]

After the CJEU's ruling in *Fidelity Funds,* the Dutch Supreme Court was asked by the CJEU if it wanted to maintain the abovementioned question.[302] This was then investigated by an Advocate General to the Dutch Supreme Court, and after his opinion on the topic was delivered, the question was retracted. In the Advocate General's view, it was clear from *Fidelity Funds* that the need to safeguard the coherence of the tax system could be relied on to justify subjecting non-resident investment funds to the same distribution requirements as resident investment funds. However, in light of *Fidelity Funds,* it was inconsistent with EU law not to allow non-resident investment funds the possibility to *voluntarily* fulfil these requirements. For this reason, the Advocate General considered that it was clear that the Dutch system was incompatible with Article 63 TFEU in that it did not make it possible for non-resident investment funds to qualify for the refund. In the Advocate General's view, non-resident investment funds should be able to qualify for this refund if they withheld tax on dividends to their members to the extent that the payments could be traced back to Dutch-sourced dividends.[303]

If similar reasoning is applied on the Swedish withholding tax system, it should not be of importance that the legislation does not explicitly mention that tax should be withheld for the favourable tax treatment to apply. Instead, it is enough that the favourable tax treatment is made subject to the redistribution of proceeds from the fund and that these proceeds are as a rule taxed at unitholder level. In the author's opinion, this should also follow from the fact that a direct link should be analysed

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[301] van Duijn and Sinnige, 'Netherlands - Corporate Taxation', *Country Analyses IBFD*, last reviewed 15 November 2018 sec 12.2.1.

[302] Schellekens, 'Netherlands - Dutch Supreme Court: AG recommends withdrawal of questions to ECJ in Köln-Aktienfonds Deka (C-156/17) and X (C157/17)', *News IBFD*, published on the 9th of October 2018.

[303] Schellekens (n 302).

in light of the objective sought with the provision at hand. This is because the purpose of the Swedish dividend distribution provision is to make sure that the taxable income is "rolled over" on the members of a CIV, even if no explicit mention of this is made in the legislation at hand.[304]

When it comes to the second counter argument, namely that it is not certain that the dividends are actually taxed at unitholder level when distributed from a Swedish intermediary, this argument is trickier to refute. In this respect, it is not entirely clear from *Fidelity Funds* whether the tax withheld on the minimum distribution was final or if it could be repaid to tax-exempt investors. The only aspect that can clearly be discerned from *Fidelity Funds* is that the withholding tax levied could sometimes be deducted against a taxpayer's share income tax liability.[305] However, in such a case the income is still taxed once, and the deduction is only used to avoid *double* taxation at unitholder level.[306] Moreover, it is not possible to gather if the Dutch withholding tax was final from the question posed by the Dutch Supreme Court.

Consequently, due to this uncertainty as to the content of the Danish and Dutch legislation, it is not entirely clear how the CJEU would assess the Swedish system, where the favourable tax treatment is made dependent on redistribution but where it is not certain that tax is actually levied at unitholder level. Possibly, just as in the initial US mutual fund cases delivered by the Court of Appeal, the existence of a direct link would be denied. However, in the author's view, due to this uncertainty it cannot either be ruled out that the need to safeguard the coherence of the tax system could be relied on in cases dealing with this legislation.[307]

Nevertheless, just as in *Fidelity Funds,* the Swedish withholding tax rules should in any case not be proportional since they make it impossible for a non-resident

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[304] See section 3.2 above.
[305] Opinion of Advocate General Mengozzi (n 252) paras 52–56.
[306] Riis and Lytken, 'Denmark - Corporate Taxation', *Country Analyses IBFD*, last reviewed on the 1st of July 2018 sec 6.1.2.
[307] See Lohela (n 36) p 45 for similar reasoning.

investment fund to qualify for the favourable tax treatment. In this regard, non-resident investment funds should also be able to qualify for this treatment (de facto exemption from tax on dividends), provided that they distribute their income and pay a Swedish tax equal to the tax that would have been withheld by a comparable Swedish intermediary in relation to Swedish-sourced dividends. This is important since it is possible for Swedish intermediaries to make certain deductions that can reduce the tax withheld on the redistributed dividend income, as was the case in *Fidelity Funds.*[308] In this context, it can also be recollected that generally US mutual funds/RICs distribute all their taxable income, which could make it easier for them to comply with a distribution requirement than for a UK OEIC.

8.3 Interim Conclusion

As a conclusion, it can be argued that it should not be possible to justify a restriction to the free movement of capital if it is found that a UK OEIC or a US mutual fund is in a comparable situation with a Swedish UCITS fund or special fund, at least under the currently applicable legislation. However, it is possible that the discriminatory treatment under the pre-2012 legislation applicable for Swedish UCITS funds and special funds, as well as the currently applicable legislation for Swedish fiscal investment enterprises, could be *justified by the need to safeguard the coherence of the tax system*. Nevertheless, this conclusion is uncertain and whatever the case may be, this latter legislation is still contrary to EU law since not allowing non-resident investment funds to fulfil the same requirements as the Swedish intermediaries cannot be *proportional* in light of the justification ground used. In the author's opinion, this follows from the CJEU's ruling in *Fidelity Funds.*

[308] It follows from Chapter 39, sec 14 of the ITA that general provisions on deductions are applicable for fiscal investment enterprises, if not otherwise stated. Examples of costs that can reduce the taxable income are interest fees and management fees, see Lodin et al., *Inkomstskatt – en läro- och handbok i skatterätt – del 2,* 2017 p 584.

9. Conclusion

The aim of this paper has been to analyse whether it is compatible with EU law to levy a withholding tax on dividends to non-EU investment companies that satisfy similar regulatory requirements as Swedish tax-exempt investment funds. The analysis has primarily focused on the Swedish treatment of two foreign investment companies: the US mutual fund and the UK OEIC (post-Brexit).

The main findings of the paper are the following. First, it has been argued that the free movement of capital (Article 63 TFEU) should generally become *applicable* in cases dealing with the Swedish withholding tax regime and third country investment funds, since the Swedish provisions apply indiscriminately to all forms of investments. Moreover, the standstill clause (Article 64 TFEU) should rarely become applicable in cases dealing with US mutual funds and UK OEICs, since most of their investments are portfolio investments.

Second, it has been claimed that UK OEICs and US mutual funds are treated *less favourably* than Swedish UCITS funds, Swedish special funds, and Swedish fiscal investment enterprises in terms of dividend taxation. Moreover, several arguments have been presented for viewing the non-EU investment companies as being in *objectively comparable situations* with either of these Swedish entities. In relation to the Swedish investment funds, this is due to that it makes more sense to focus on the material criteria that these entities must fulfil, than any formal criteria, under the purpose approach adopted by the CJEU in its case law. Moreover, in relation to Swedish fiscal investment enterprises, this is because it is inconsistent with CJEU case law to require that a foreign entity must be a “Swedish company limited by shares” to qualify for the favourable tax treatment. Nevertheless, it should be compatible with EU law to require that a foreign entity fulfils the other criteria in the ITA, including the criterion of almost exclusively investing in securities, for comparability with a Swedish fiscal investment enterprise to be established.

Third, *justification* may come into question if a UK OEIC or a US mutual fund is compared to a Swedish UCITS fund or a Swedish special fund, under the legislation that existed before 2012, or to a Swedish fiscal investment enterprise. Still, this conclusion is uncertain and whatever the case may be, the legislation is still not *proportional* in light of the justification ground used (the need to safeguard the coherence of the tax system).

As a conclusion, this paper has shown that there is no clear answer as to how the CJEU would assess the Swedish withholding tax regime's treatment of non-EU investment companies. For this reason, the summary of the findings provided here is also full of *"shoulds", "mays",* and "*it makes senses".* Nevertheless, it is still possible to criticise the current Swedish lower court practise for mainly focusing on the distinguishing criteria laid down in the legislation assessed, including legal form requirements, and not on whether the sole focus on legal form is compatible with the actual purpose of the legislation.

As a final comment, it can be highlighted that if the current Swedish interpretation of EU law is wrong, Sweden risks having to repay large sums of illegally withheld dividend tax to non-UCITS (including non-EU) investment companies. In this context, it can especially be mentioned that the CJEU has not agreed to limit the temporal effects of its judgments in any of the cases looked at, despite the concerned Governments' arguments that it would have grave financial consequences not to do so.[309] For this reason, it is in the interest of Sweden to settle the uncertainties regarding the Swedish withholding tax system and its treatment of non-UCITS investment companies as soon as possible. As such, it is welcome that leave to appeal was granted by the SAC in the latest US mutual fund case assessed by the Court of Appeal.[310] It can only be hoped that, as a next step, the SAC requests a preliminary ruling from the CJEU.

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[309] See e.g. *Santander* (n 142) para 6, *Commission v Belgium* (n 1) para 91 and *Emerging Markets* (n 1) para 112.

[310] SAC protocol from the 14th of March 2019 in case 3725–3727-18.

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