



Update: Dividend withholding tax - South Africa & the Netherlands

A Dutch lower court recently ruled that dividend payments from the Netherlands to South African corporate entities with 10% or more ownership in the company are not subject to Dutch dividend withholding tax. This means that South African shareholders are in principle entitled to a refund of the unduly Dutch dividend withholding tax paid. An appeal has however been lodged by the Dutch Tax authorities.

The court case exposes an interesting technical issue on the application of Most-Favoured-Nation (MFN) clauses as it reviews the date of entry of the reduced withholding tax rate in the treaties between South Africa and the Netherlands and South Africa and Sweden.

Arguments also exist that a 0% dividend withholding tax rate should apply in the reverse situation (dividend distribution by a company in South Africa to a Dutch shareholder). Please note however that in the view of the South African Revenue Services (SARS) the MFN clause of the Protocol could not avail to a 0% dividend tax rate.

We advise Dutch and South African taxpayers to (i) review whether they have paid dividend withholding tax in recent years and to (ii) consider distributing a dividend on a short notice, as the window for the 0% dividend withholding tax rate is expected to be limited.

In 2005 the governments of South Africa and the Netherlands concluded a tax treaty to avoid double taxation (hereinafter: "Treaty"). The Treaty entered into effect on 28 January 2008. With respect to the treatment of intercompany dividends, both countries agreed to the following. In principle the dividend withholding tax rate is reduced to 5% under the Treaty (if the shareholder is a corporate entity with more than 10% ownership). A MFN clause is included in the Treaty as per 2008 (by protocol). The MFN clause is a mechanism that arranges that if an agreement between South Africa and a third country is more favorable than the arrangements with the Netherlands, this favorable arrangement automatically applies under the Treaty from the moment the other agreement is concluded. There are arguments that the MFN clause in the Treaty has no direct beneficial effect due to limitation in time wording in the clause, therefore parties looked at the MFN clause in the South Africa – Sweden tax treaty.

In 1995 Sweden and South Africa concluded a tax treaty in which no dividend withholding tax was due in case the shareholder was a corporate entity with 25% or more ownership in the company. In 2012 South Africa introduced dividend withholding tax in its legislation. As a consequence several tax treaties have been renegotiated. As per 18 March 2012, the tax treaty between South Africa and Sweden was amended with respect to the dividend article. Both parties agreed that 5% dividend withholding tax due if the shareholder is a corporate entity with more than 10% ownership. Also, a MFN clause was included. South Africa also concluded treaties with Cyprus (1998), Oman (2003) and Kuwait (2006) in which no dividend withholding tax is due if conditions are met.

As a result of the MFN clause in the tax treaty between South Africa and Sweden, parties in the Dutch court case agreed as an undisputed fact that the 0% rate also applies as the protocol does not contain a limitation in time with respect to the date of conclusion of the reference tax treaty with a third state. It is interesting however that the Swedish tax authorities may however not agree with



this explanation by the parties in the Dutch court case. We understand that from a Swedish perspective the reduced withholding tax rate does not apply because no treaty, which is more beneficial, has been concluded after the MFN clause was included in 2012.

The taxpayer argued in the court case that no dividend withholding tax should be due on dividend distribution between South Africa and the Netherlands based on the MFN clause in the Treaty and furthermore taking into account the MFN clause in the amended tax treaty between South Africa and Sweden. The lower court accepted this tiered approach and ruled that as from 18 March 2012 the 0% dividend withholding tax is applicable. The Dutch tax authorities have filed an appeal to the judgment which is currently pending.

In principle relevant companies should be able to recover the Dutch withholding tax paid per 18 March 2012. However, Dutch law requires that a refund request must be done within three years after the end of the financial year in which the dividend was distributed to safeguard its rights. Therefore the period for refunds is limited.

Although this is a Dutch case regarding the Dutch dividend withholding position under the Treaty, there are good arguments that a similar position as taken by the taxpayer in this court case could apply in the reverse situation (i.e. if a South African subsidiary distributed dividends to its Dutch beneficial owner and dividend withholding tax is or will be paid). SARS however believes that 0% dividend withholding tax rate is not applicable between the Netherlands and South Africa because the Kuwait – South Africa treaty was signed before the Treaty. Up to the present time, SARS has not provided further clarity on this subject.

South Africa has indicated that it intends to renegotiate all its treaties in which a 0% dividend withholding tax rate is concluded. Please note that the treaties between South Africa and Cyprus (2015) and between South Africa and Oman (2013) already have been renegotiated and a 5% dividend withholding tax rate was included by protocol. Please find below an overview of all the South African treaties that can undo the effect of a positive Dutch court judgment for future dividend distributions (the change of only one tax treaty is sufficient) and their status.

Kuwait

We understand from the latest status (updates included up to 11 February 2016) that the negotiations are in the process of being finalized.

The Netherlands

Currently, the Netherlands and South Africa are renegotiating their tax treaty. At the moment it is uncertain if and when a new treaty will be agreed upon.

Sweden

Currently, we are not aware of renegotiations or a new tax treaty concluded between Sweden and South Africa.

A word of caution: whilst the application of the MFN clause may effect in a 0% dividend withholding tax rate, the included “main purpose” and “beneficial owner” clauses in the Treaty still apply. Companies should therefore carefully consider their tax structure and implement sufficient substance in the Netherlands (South Africa in the reversed situation) and avoid artificial structures.



The Dutch court case offers opportunities to claim a refund of Dutch dividend withholding tax which a South African shareholder incurred in recent years. We can assist you with a review of the companies' tax position and assist with the refund procedure to safeguard the companies' rights. However, please note that the outcome of the pending appeal might be different.

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We advise all parties to safeguard their rights and to await the final judgment in this case. It can also be considered to distribute dividends before the relevant treaties are amended. Please note that timely action is recommended, since South Africa is renegotiating its tax treaties with a 0% withholding tax rate on dividends and also considering the deadlines for filing the refund claim.

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