TAXATION OF DIVIDEND IN THE EUROPEAN UNION – A COMPARATIVE STUDY

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Abstract: *The aim of this contribution is to identify the criteria and to classify the Member States of the European Union into individual groups based on the rules for dividends taxation. The paper focuses on selected rules for taxation of domestic and also dividends received from other EU Member States in case of tax residents – legal entities. The selected taxing rules for the dividend income were monitored over three time periods, namely years 2016-2018 . Based on the comparison made, it was found out that there is a variability among EU Member States´ legal regulations. On the other hand, EU Member States can be divided into several groups that show, if not directly identical, very similar parameters for the taxation of the categories of dividends in question. As regards the exemption of dividends from taxation, the EU Member States´ legal regulations set three options: exemption without any conditions laid down, exemption conditioned by meeting the criteria set on the part of the taxable person, or partial exemption of 95 % of that income. Dividend income that are not exempt due to non-compliance with the conditions set are taxed either within the global tax base or in a separate tax base.*

Keywords: *Tax Resident, European Union, International Taxation of Dividends.*

JEL classifications: *H25, H26.*

1 INTRODUCTION

Dividends in general represent profits generated by companies and distributed to shareholders (Parker et al., 2009) in the form of cash dividends or stock dividends (Parua and Gupta, 2009). Stock dividend "*is a dividend paid in shares of stock instead of cash, and is properly payable only out of surplus profits*" (Business World, 1998). The amount of the dividend is determined by dividend policy (Abbadi et al., 2016), which can be defined as a compromise between the size or earned and undivided profit and divided cash or securities (Parua and Gupta, 2009). The most important factors influencing dividend policy can be deemed to be cash flow stability, availability of profitable investment opportunities, controlling matters regarding corporate ownership structure and continuity of previous dividend payments (Pourheydari, 2009). The dividend policy further represents an important factor in evaluation of firm value, and tax rates in particular are used to determine its influence (Ince and James, 2009 in Khalid and Ur Rehman, 2015). However, such influence does not always have to be positive: for instance, according to Black's study (1976), the distribution of dividends has a negative impact on the firm value if their taxation is taken into account.

Taxation of dividends further has an impact on investment incentives (Khalid and Ur Rehman, 2015). A high tax rate has a negative impact on dividends, while investors whose dividend income is exempt from the tax, try this influence and get higher dividend (Tehmina Khan, 2005 in Khalid and Ur Rehman, 2015). In this regard, legal regulation of dividend taxation therefore plays an important role: it can be viewed as one of the key factors together with investment decisions on the location or re-location of a company's headquarters. There are many reasons for this. Some states have not yet adopted certain more stringent rules for the taxation of profits in relation to a controlled foreign company ("*Controlled Foreign Company rules*"), or provide certain advantages to shareholders in the taxation of dividends - lower tax rates, exemption from tax, etc. (Pihlgren and Weije, 2010). Stunda's study (2016) even showed a mutual dependence between the tax rate and share prices. According to conclusions drawn in this study, a low tax rate triggers share price growth notwithstanding company size.

The situation is highly specific in the European Union (the "EU") where provisions of law of the member states are also regulated by EU law – both primary and secondary. In primary law, this means in particular the free movement of capital pursuant to Article 63 of the Treaty on the Functioning of the EU and the right of establishment pursuant to Article 49 of the Treaty on the Functioning of the EU (Eur-lex, 2018a). As regards secondary law, this means *Council Directive 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States* (hereinafter referred to as "2011/96/EU Directive") (Eur-lex, 2018b).

This article focuses on the situation in the EU. Its objective is to compare selected rules for the taxation of dividends of tax residents of member states of the European Union, namely, legal entities, in 2016-2018. A contribution presented at a conference, "*DANĚ -TEORIE A PRAXE 2017" (TAXES* -

THEORY AND PRACTICE 2017) forms the core of this article, expanded by a further time period.

2 OBJECTIVE AND METHODOLOGY

The objective of this contribution is to identify criteria, and subsequently, to classify member states of the European Union into individual groups based on their rules for the taxation of dividends. Specifically, the article focuses on basic rules for the taxation of national dividends, as well as dividends received from other EU member states by tax residents - legal entities. An individual objective is to compare such basic rules for the period of 2016–2018. General rules for the taxation of dividend income, stipulated with regard to cash dividends, are always in force and effect as of June 1 of the relevant taxation period. Rules relating to stock dividends, set forth by the legislation of some EU member states, were not taken into account.

Based on an analysis of selected sources (Eur-lex, (2018b); PwC (2016); PwC (2017), PwC (2018), Russo et al. (2007)), individual criteria were identified to which the existent variants were subsequently assigned. The matrix provided below (see table 1 below) served as a basis used to classify states by means of the criteria defined.

Table 1: Comparative criteria

	Criterion	Variants
Tax base	Determination of tax resident base	• Territorial • Global
Taxation of dividends	Method of taxation of national dividends	• Exempt without any restrictive conditions • Exempt subject to conditions of a minimum share of 10% held for at least 1 year *Note: the variant was chosen as a benchmark, these are criteria stipulated by Czech legislation* • Exempt subject to conditions other than a minimum share of 10% and/or held for at least 1 year • Partly exempt up to 95%, provided certain conditions are met; the balance is subject to corporate tax • Income subject to corporate tax (unless the legal entity meets conditions for exemption) • Income taxed by inclusion into a separate tax base (if the legal entity does not meet conditions for exemption)

Method of taxation of dividends received from EU member states	• Exempt without any restrictive conditions • Exempt subject to conditions of a minimum share of 10% held for at least 1 year *Note: the variant was chosen as a benchmark, these are criteria stipulated by Czech legislation* • Exempt subject to conditions other than a minimum share of 10% and/or held for at least 1 year • Partly exempt up to 95%, provided certain conditions are met; the balance is subject to corporate tax • Income subject to corporate tax (unless the legal entity meets conditions for exemption) • Income taxed by inclusion into a separate tax base (if the legal entity does not meet conditions for exemption)
Tax rates	• Corporate tax (general tax rate) • Tax rates applicable to separate tax base

Source: Own elaboration, with reference to PwC (2016), PwC (2017), PwC (2018), (Eur-lex, 2018b), Russo et al. (2007).

The results of the above analysis of the relevant sources are presented in the following chapter. The final summary is preceded by discussion, in which selected issues are outlined, together with certain options for further research in this area.

3 RESULTS

The taxation of dividends is regulated by international, EU and national laws. In international law, this means "only" double taxation treaties, which are based on model agreements. Of primary importance in this regard is the OECD model treaty (for the up to date version, see OECD (2017)). As regards taxation rules in the state of tax residence of the dividend recipient, the OECD model treaty merely stipulates that the state of tax residence is authorized to subject the relevant income to tax. This rule is incorporated into the relevant individual treaties. Therefore, the state of residence of the dividend recipient is not limited in this regard - the double taxation treaties provide for the right, rather than duty, to subject such income to tax.

In EU law, international taxation of dividends is regulated by both primary and secondary law. In secondary law, this involves, as noted above, Directive 2011/96/EU which regulates the taxation of dividends distributed between parent companies and subsidiaries of different member states. The directive sets forth conditions on which such dividend income is exempt (the basic criteria have to do with the duration of possession, interest size and legal forms - see in particular Articles 2 and 3 of Directive 2011/96/EU) (Eur-lex, 2018b). However, the way in which the conditions are defined gives the states a great deal of discretion, which, as shown by the results attained, the member states use.

Despite the relatively high degree of discretion for national legislation, the influence of primary law cannot be disregarded. It happens through the case law of the Court of Justice of the European Union. In its decisions, the Court of Justice of the EU provides interpretations of EU law, including in the context of dividend taxation in relation to fundamental freedoms (for details, see Bělušová, Brychta, 2017).

One of the few aspects of international taxation of dividends which is not determined by EU or international law in EU member states is the way in which the tax resident's tax base is determined. Most member states provide for "unlimited tax liability" for their tax residents - i.e., a situation where the tax resident reports its global income for the purpose of taxation in the country of tax residence. Only Romania stipulates a "limited tax liability" for its tax residents. This means that a tax resident of Romania only reports territorial income - i.e., income from sources in Romania - for taxation purposes.

Table 2 provided below divides EU member states according to rules for the exemption of national dividend income during the period under observation. The comparison made, the result of which are provided in the table, shows that legislation pertaining to the taxation of dividends appears to be stable, i.e., no legislative amendments have occurred with regard to the rules. However, the results of the below classification manifest a certain variability as regards the criteria under observation.

Thirteen member states stipulated in its legislation that national dividend income is exempt from tax regardless of the size of the shareholding or without the length of the holding period, or rather, that they are not subject to tax. Specifically, the legislation of the following countries contains such provisions: Austria, Bulgaria, Cyprus, Finland, Croatia, Hungary, Ireland, Latvia, Poland, Romania, Sweden, Slovakia, and the Great Britain.

Three member states - Czech Republic, Portugal and Lithuania - adopted limits in the form of minimum shareholding of 10% and minimum holding period of 1 year into their legislation.

Table 2 Classification of EU member states according to available exemption from national dividend taxation in 2016-2018

Type of exemption	States					No. of states
Exempt without any restrictive conditions	AT	BG	CY	FI	HR	(13/28)
	HU	IE	LV	PL	RO	
	SE	SK	UK			
Exempt subject to conditions of a minimum share of 10% held for at least 1 year	CZ	LT	PT			(3/28)
Exempt subject to conditions other than a minimum share of 10% and/or held for at least 1 year	DK	EE	EL	ES	LU	(7/28)
	MT	NT				
Partly exempt up to 95%, provided certain conditions are met; the balance is subject to corporate tax	BE	DE*	FR	IT*	SI*	(5/28)

Source: Own elaboration, with reference to PwC (2016), PwC (2017), Pwc (2018), Deloitte (2016). Deloitte (2017), Deloitte (2018)

* Exempt up to 95%, without conditions

Abbreviations used:

AT – Austria, BE – Belgium, BG – Bulgaria, CY – Cyprus, CZ – Czech Republic, DE – Germany, DK – Denmark, EE – Estonia, EL – Greece, ES – Spain, FI – Finland, FR – France, HR – Croatia, HU – Hungary, IE – Ireland, IT – Italy, LT – Lithuania, LU – Luxembourk, LV – Latvia, MT – Malta, NL – Netherlands, PL – Poland, PT – Portugal, RO – Romania, SE – Sweden, SI – Slovenia, SK – Slovakia, UK – United Kingdom.

Exemption on conditions other than a minimum shareholding of 10% and minimum holding period of 1 year is stipulated by the legislation of 7 member states, specifically, Denmark, Estonia, Greece, Spain, Luxembourg, Malta and the Netherlands. The legislation of Malta and the Netherlands stipulates that national dividend income is exempt if the shareholding is at least 5%. Estonian and Danish legislation also provides only for the condition concerning the size of the shareholding, however, for the dividend recipient - tax resident - to be able to claim exemption, it must have a shareholding of at least 10%. The remaining three member states, i.e., Spain, the Netherlands and Greece, stipulate both a condition concerning the size of shareholding and a condition concerning the length of holding period. Spanish legislation stipulates the following conditions for exemption: a minimum shareholding of 5%, or shareholding value of at least EUR 20 million, and the length of the holding period for 12 months. Dutch legislation stipulates a minimum shareholding of 10%, or shareholding value of at least EUR 1.2 million, and the length of the holding period for 12 months. National dividends received by a tax resident - legal entity - of Greece are exempt of corporate tax only if the company has a 10% share for 24 months in the company distributing the dividend.

The legislation of five member states - Belgium, Germany, France, Italy and Slovenia - provides for a partial exemption of dividend income without any conditions. French tax residents can claim exemption for national dividend income if they hold a share of at least 5% for the period of two years. Belgian tax residents need to hold a 10% interest, or an interest worth at least EUR 2.5 million, for 1 year.

Table 3 below provides a classification of EU member states based on dividend taxation where the entity did not qualify for exemption over the period under observation. The results indicate that the stipulation of the taxation method is a stable part of national legislation.

Table 3 Classification of EU member states upon non-compliance with conditions for exemption of national dividends in 2016-2018

Method of taxation dividend	States					No. of states
Corporate tax (general tax rate)	BE	DE	DK	EE	EL	(14/28)
	ES	FR	IT	LT	LU	
	MT	NT	PT	SI		
Tax rates applicable to separate tax base	CZ					(1/28)

Source: Own elaboration, with reference to PwC (2016), PwC (2017), Pwc (2018), Deloitte (2016). Deloitte (2017), Deloitte (2018).

In 10 member states, income from dividends which did not qualify for exemption are included in the tax base of the tax resident and are subject to corporate tax. In the Czech Republic, such income is taxed in a separate tax base.

Table 4 below presents a classification of EU member states according to type of exemption in relation to dividends received from other member states during the period under observation. This classification shows that even where intra-community dividends are taxed on the part of beneficiaries - tax residents - legal entities, no changes had occurred that would impact the rules under observation.

Table 4 Classification of EU member states according to type of exemption in relation to dividends received from other member states in 2016-2018

Type of exemption	States	No. of states
Exempt without any restrictive conditions	BG CY HR HU LV PL SK UK	(8/28)
Exempt subject to conditions of a minimum share of 10% held for at least 1 year	CZ FI LT PT RO SE	(6/28)
Exempt subject to conditions other than a minimum share of 10% and/or held for at least 1 year	AT DK EE EL ES IE LU MT NL	(9/28)
Partly exempt up to 95%, provided certain conditions are met; the balance is subject to corporate tax	BE DE* FR IT* SI*	(5/28)

Source: Own elaboration, with reference to PwC (2016), PwC (2017), Pwc (2018), Deloitte (2016). Deloitte (2017), Deloitte (2018).

* Exempt up to 95%, without conditions

The comparison shows that the legislation of eleven EU member states provides for exemption or exclusion from taxation of dividends received from other EU member states, notwithstanding the size of the shareholding and without the length of the holding period. This is true for legislation of the following states: Bulgaria, Cyprus, Hungary, Latvia, Poland, Slovakia and the Great Britain.

Exemption upon satisfaction of conditions – a shareholding of at least 10% and the length of holding period for at least 1 year can be found in the legislation of six member states – the Czech Republic, Finland, Lithuania, Portugal, Romania and Sweden.

Exemption upon satisfaction of conditions other than those mentioned above can be found in the legislation of 9 member states, namely, Austria, Denmark, Estonia, Greece, Spain, Ireland, Luxembourg, Malta, the Netherlands. The legislation of Ireland, Malta and the Netherlands only exempts dividend income if the recipient - tax resident - legal entity holds a minimum 5% shareholding in the company distributing the income. Domestic legislation of Austria, Denmark and Estonia provide for such exemption for holdings of at least 10%. The remaining countries, i.e., Spain, Greece and Luxembourg provide for both the size of the shareholding and the duration of possession. Luxembourg legislation provides for exemption If a 10% interest, or an interest worth at least

EUR 1.2 million, is held for 12 months. Greek legislation works with a 10% shareholding, however, for the tax payer to be exempt, the interest must be held for 24 months. Exemption under Spanish law applies to 5% shareholdings, or shareholdings worth at least EUR 20 million, held for 1 year.

A partial exemption equivalent to 95% of income was adopted by 5 member states. Once again, Italy, Germany and Slovenia adopted such exemption in their legislation without any conditions as to a minimum shareholding or duration of possession. Under Belgian law, the same conditions apply as those for national dividends, i.e., a minimum shareholding of 10% or acquisition price of shares in excess of EUR 2.5 million, held for 1 year. In France, a partial exemption of dividend income applies if the condition of a minimum shareholding of 10% of the company is satisfied. French law does not provide for the duration of possession. The methods of dividend taxation if the conditions for exemption are not satisfied during the relevant 3-year period are provided in Table 5 below.

Table 5 Classification of EU member states according to the system of taxation of dividends received from other EU member states, which do not qualify for exemption, in 2016-2018

Method of taxation dividend	States					No. of states
Corporate tax (general tax rate)	AT	BE	DE	DK	EE	(18/28)
	EL	ES	FI	FR	IE	
	IT	LT	LU	MT	NT	
	PT	SE	SI			
Tax rates applicable to separate tax base	CZ	RO				(2/28)

Source: Own elaboration, with reference to PwC (2016), PwC (2017), Pwc (2018), Deloitte (2016). Deloitte (2017), Deloitte (2018)

The results shown indicate that no changes have occurred in the legislation of the member states over the relevant time period, where such changes would impact such classification. Income from dividends received from other member states, which did not qualify for exemption, are to be included in the tax base of the tax resident and taxed at corporate tax rate in 18 member states. Two member states - the Czech Republic and Romania - stipulated that such income is to be included in a separate tax base.

The rates of taxation of dividend income in individual member states are provided in Table 6. These apply to both types of dividends - both national and those received from another member state as of June 1, 2018

Table 6 Tax rates in force as of June 1, 2018

5 % RO	12,5 % IE	15 % CZ	18 % nebo 15 % LU	19 % SI, PL
20 % EE, FI	22 % DK	22,83-36,8 % DE	24 % IT	25 % ES, NL, DE, AT
29 % BE, EL	33,33 % FR	35 % MT		

Source: Own elaboration, with reference to PwC (2016), PwC (2017), Pwc (2018), Deloitte (2016). Deloitte (2017), Deloitte (2018)

Unlike general rules for taxation of national or intra-community dividend income, corporate tax rates have changed during the period under observation. Slovenia increased the corporate tax rate in its legislation from 17% to 19% as of January 1, 2017. Contrary to that, Italy reduced its rate from 31.4% to 24% in the same year. Corporate tax rate was also modified in Luxembourg legislation as of January 1, 2018, specifically, from 21% to 18%, and from 20% to 15%. This declining trend can be observed in the same year also in Belgian legislation, where a reduction from 33.99% to 29% was made.

4 DISCUSSION AND CONCLUSIONS

The basic rules which were compared over a period of three years were in force and effect always as of June 1 of the relevant calendar year. General rules were stipulated for cash dividends, i.e., special rules which apply to stock dividends and which are provided for in the laws of some EU member states were not taken into account. Selected rules pertaining to the taxation of national and intra-community dividend income were surveyed.

The analysis showed that the taxation of the relevant type of income can be considered relatively constants. However, the author of this article expects that in light of *Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market*, certain changes will occur in the legislation of the individual states. Such legislative changes which will concern the taxation of earned and undivided dividend income only apply to companies which will be deemed to be controlled foreign companies pursuant to the definition set forth in the directive (see Eur-lex, 2018c).

Nevertheless, for the sake of protection against aggressive tax planning, certain member states adopt conditions in their legislation which apply to exemption of dividend income received in relation to foreign companies with their registered seats in third countries. Exemption is thus conditioned on the satisfaction of the applicable conditions. The analysis showed that such conditions relate in particular to the tax burden on the part of companies distributing the dividends. Cypriot legislation can be mentioned as an example: the recipient of the dividend – tax resident– legal entity only qualifies for exemption if the company distributing the dividend income is subject to a significantly higher tax rate in the country of its residence, as compared to the tax burden in Cyprus (i.e., effective tax rate higher than 6.25%) (PwC, 2018). The assessment of benchmarks in relation to third countries provides room for follow-up research.

Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB). should also contribute to the fight against aggressive tax planning, however, its adoption, in light of Article 8 of the draft, should not impact heretofore results of the survey, unless the companies are classified as controlled foreign companies (for the definition, see Article 59) (Eur-lex, 2018d). Despite that, according to Ortmann and Sureth-sloane (2016), taxation of dividends, together with taxation of interest and options for reflecting losses, has a significant impact on tax subjects deciding whether to use a common consolidated tax base (CCCTB) and on their potential selection of tax systems. The above facts and the results of the analysis show that tax systems within member states are becoming more and more alike under the initiative of the European Union (Gerritsen and Kuipers, 2017); nevertheless, the author of this article believes despite that that certain variability will survive in their laws. Tax competition can be expected to continue in this area as well. This is undoubtedly an aspect tax payers will appreciate because they profit from it.

As regards future developments, pending legislative changes will presumably have a considerable impact (factual implementation of the BEPS plan), and so will Brexit. The author of this article is of the opinion that it can be expected to have a broader impact, perhaps including a stronger tax competition in the effort to attract capital. Due to Brexit, current legal regulations, pursuant to which dividends received from other EU member states were exempt from tax, will no longer apply. It is thought that such dividend distributions will then be subject to a 5% withholding tax. (Treatment, 2017)

In the context of this topic, one must not forget about case law of the Court of Justice of the European Union, by now rather extensive. If recipients of dividends are in comparable positions, the different treatment under domestic law results in a breach of fundamental freedoms (Ernst and Young, 2013). However, the decision of the Court of Justice of the European Union equally applies to dividends received from third countries (for details, see Bělušová, Brychta, 2017). If further aspects, such as the issue of dividends received from third countries, prevention of double taxation and issues related to abuse of the law, are included in these contemplations, the area and complexity of research inevitably increases greatly. There is ample room for research also in the area of a more detailed research of the legislation of member states in conjunction with the relevant statistical data.

Redemption of shares and its taxation is also worth mentioning in connection with a more in-depth analysis of the legislation of member states. This is due to the fact that cash dividends and redemption of shares are two tools a company can use to pay shares in profit to its shareholders (Bechmann, Raaballe, 2006). Such action is caused in particular by the regime of capital gains taxation (Allia et al., 1993, Allen and Michaely (2003) and Bernhardt et al. (2005) in Kao and Chen (2011), which is more advantageous that the taxation of dividend income. Nevertheless, redemption of shares is prohibited within the European Union (see *Second Council Directive 77/91/EEC of 13 December 1976 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent)* However, the directive provides for a certain degree of discretion even in this case, and its application makes it possible to extend the research

This research focused on a relatively small area which can be viewed as a basis for follow-up research. Specifically, it focused on the identification of rules for the taxation of dividend income of EU tax residents (legal entities) and a subsequent classification of EU member states according to selected criteria. Attention was directed both at the rules for the taxation of national dividends, and the taxation of dividends received from other EU member states. The relevant rules were assessed over a period of three years. The comparison carried out shows that there is a certain degree of variability between the provisions of law of the individual member states. On the other hand, EU member states could be divided into several groups which manifest if not identical, then very similar parameters for the taxation of the relevant dividend categories. Thirteen member states have provisions of law which provide for the exemption of such income regardless of the duration of possessions or the size of the interest in the relevant company, ten member states have exemption of income subject to the satisfaction of stipulated conditions, and five member states a partial exemption at the level of 95% (three member states without any conditions, two member states subject to the satisfaction of stipulated conditions). As regards dividends received from other EU member states, unconditional "exemption" is provided for in eight member states, exemption subject to the satisfaction of stipulated conditions in fifteen member states, and a partial exemption at the level of 95% in five member states (in three member states without any conditions, in two member states subject to the satisfaction of stipulated conditions).

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