

ECJ says no to double non-taxation

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There are numerous [reports](#) this morning on the ruling of the European Court of Justice yesterday that appears to have allowed the UK to continue its tax treatment of dividend payments within groups of companies which appear to discriminate across borders. Dividends paid within UK groups are tax exempt on the recipient. It was presumed by the litigants (British American Tobacco in this case) that this should mean that dividends from overseas subsidiaries should also be exempt from tax when received by a UK parent company.

The welcome news is that the ECJ does not agree. It has said that so long as there is freedom of establishment within the EU, and freedom of movement the UK's tax system did not contravene EU law so long as there was a sufficiently favourable tax rate and credit system to mitigate double taxation.

No one expected this, although there had been welcome signs of a shift in ECJ attitudes towards tax over the last year meaning which have meant that instead of almost invariably finding for the taxpayer, as they did until 2005 they now as often find for governments. The reason in this case is obvious. The rights that were being balanced were those of the taxpayer and state. And the ECJ knew that the taxpayer was effectively asking for the right to non-taxation because by using tax havens and participation exemption countries such as the Netherlands it would be relatively easy for large parts of a company's income stream to be made tax free if the ability of the UK to tax foreign source dividends was removed. This is precisely why so many flat tax proponents see the [non-taxation of foreign source](#) income as one of the major advantages for them of that tax.

Instead the ECJ has said quite clearly that the State has a right to tax. Accountants are up in arms in horror. Look at this series of quotes [from the FT](#):

Jonathan Bridges, of KPMG, the professional services firm, said that the ruling potentially introduced "yet another layer of complexity into the UK's already overly

cumbersome corporate tax system".

Jason Lester, a partner in Ernst & Young's international tax services team, said there was a "distinct lack of clarity as to the approach the UK courts should adopt when considering this matter further".

Bill Dodwell, of Deloitte, said: "On the key issue of whether a system of double tax relief is acceptable, confusion reigns."

This is untrue. Confusion does not reign. What is true is that the right to double non-taxation has not been granted. That's quite different. These accountants show their true colours by commenting as they do. Meanwhile the FT also reported that:

Richard Baron, head of taxation at the Institute of Directors, said that exempting foreign dividends could ultimately have a beneficial impact on tax revenues.

"If the government chooses to exempt all dividends received by companies, the UK's attractiveness as a location for group holding companies will shoot up. In addition, a vast amount of pointless administrative work will be saved."

That, as is normal with IoD, is disingenuous. The saving would be in tax by companies, the paperwork saving would be in the government not collecting tax due to it.

Commonsense has prevailed. The right of a government to collect tax has been asserted. It gives me considerable confidence that the [new rules](#) on controlled foreign companies will also survive legal challenge. The right of capital to roam the globe in search of low tax rates is being curtailed. Just in time, I say.