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The Court of Justice of the European Union rules on the neutralisation of the Spanish withholding tax discrimination affecting US RICs: the iShares case (C-139/25)

I. Background

On 17 September 2026, the Court of Justice of the European Union (the “CJEU”) delivered its judgment in Case C-139/25, iShares Europe ETF (the “Judgment”), in response to a question referred by the Spanish Supreme Court (order of 11 February 2025).

iShares Europe ETF (“iShares”), a US Regulated Investment Company (“RIC”), received dividends from Spanish companies during 2007 to 2010, subject to a 15% withholding tax under the Spain-US tax treaty. Spanish investment funds meeting equivalent conditions are instead taxed at 1% on the same dividends. iShares claimed a refund of the difference, arguing this disparity breached the free movement of capital under Article 63 TFEU.

The Central Economic-Administrative Court and, on appeal, the Spanish National High Court considered the case. The National High Court ruled in favour of iShares in September 2022, finding the discrimination had not been neutralised. The State Advocate’s Office appealed to the Supreme Court, arguing that iShares could, in principle, have elected to be taxed in the US in its own name and deduct the Spanish withholding tax in full, even though it chose instead to pass its income and the related tax credit through to its investors under the US “pass-through” regime applicable to RICs.

Given the number of pending cases raising the same issue, the Supreme Court stayed its decision and referred the matter to the CJEU, asking, in essence: is it enough that the fund itself could, in theory, have neutralised the extra Spanish tax, even if it never did so because it passed the income and credit on to its investors, or must actual neutralisation at investor level be proven?

II. The CJEU’s ruling of 17 September 2026, Case C-139/25, iShares Europe ETF

Considering the preliminary ruling request issued by the Spanish Supreme Court, and the question itself made by the Supreme Court, the CJEU confirmed, consistent with its own precedent, that taxing dividends paid to non-resident funds at 15% while resident funds pay 1% is a restriction on the free movement of capital prohibited by Article 63 TFEU. It expressly rejected Spain’s argument that there is no restriction simply because the non-resident fund is fiscally transparent and passes the tax burden on to its investors: what matters is that Spain, in exercising its own tax jurisdiction, imposes a heavier burden on the non-resident fund’s dividends than on a resident fund’s dividends.

Furthermore, the CJEU accepted, in line with earlier case law, that a bilateral tax treaty can neutralise this kind of discrimination. However, it set a strict test: neutralisation only occurs if the treaty allows the excess Spanish tax to be deducted in full, in every case, from the tax otherwise payable elsewhere. A mechanism that only sometimes achieves full relief is not sufficient.

The Court held that the mere fact that a fund could, in theory, have elected a tax regime allowing it to deduct the Spanish withholding tax in full does not neutralise the discrimination if the fund did not in fact make that election. Because iShares opted for the US pass-through regime and transferred the dividends and the associated tax credit to its investors, any deduction at the fund’s own level was purely theoretical, and the discrimination was not neutralised at that level. The Court added that a fund cannot be denied treaty protection

merely because it lawfully chose a tax regime that was available to it, provided that choice was not abusive or fraudulent.

The CJEU did not close the door on neutralisation altogether. It noted that the Spain-US treaty may allow the fund's investors, rather than the fund itself, to use the Spanish tax as a credit against their own tax. If that is established, and if it allows the investors to deduct the full excess tax in their country of residence, then the discrimination is neutralised at investor level. Whether that is actually the case is a question of fact and of interpretation of the treaty, which the CJEU leaves entirely to the Spanish Supreme Court to determine.

By shifting the analysis from a theoretical possibility to an effective, fully-proven outcome for the fund's investors, the CJEU has turned this into an evidentiary question: can it be shown that the investors actually obtained a full offset of the Spanish tax? The Spanish Supreme Court has consistently held that the burden of proving neutralisation lies with the Spanish tax authorities, not with the taxpayer; however, we cannot know whether the Supreme Court might change its view with respect to this specific type of taxpayer and claim. This allocation of the burden of proof will be critical in how the pending cases are ultimately resolved.

III. Impact on pending and future cases

This Judgment is directly relevant to a very significant volume of withholding tax litigation currently pending in Spain, at every stage of the process:

- i) Claims pending before the Spanish Tax Agency ("AEAT"). These claims can now be argued on the basis that the discrimination is confirmed and that neutralisation requires actual proof of a full offset at investor level, not a merely theoretical possibility at fund level.
- ii) Appeals pending before the Central Economic-Administrative Tribunal ("TEAC"). The same reasoning will apply, reinforcing the argument that the Administration must affirmatively prove neutralisation rather than assume it.
- iii) Appeals pending before the National High Court. Courts will need to apply the Judgment's evidentiary standard when assessing whether the specific facts of each fund show effective neutralisation at investor level.
- iv) Around 80 cassation appeals pending before the Supreme Court. These are directly and immediately affected, as the Supreme Court must now apply the CJEU's criteria to resolve them, including the iShares case itself.

The Judgment is equally important for future claims. Depending on how the Supreme Court applies the CJEU's criteria, particularly on which party bears the burden of proving (or disproving) neutralisation at investor level and what evidence will be considered sufficient, tax claims by non-resident funds could become considerably easier, or considerably harder, to win going forward. The forthcoming Supreme Court ruling in the iShares case itself will be the first and most important signal of how this standard will be applied in practice.

IV. Next steps

We are closely monitoring the Supreme Court's forthcoming ruling in the iShares case, which will apply the CJEU's criteria for the first time and is expected to guide the resolution of the pending cassation appeals and, indirectly, all earlier-stage proceedings. We recommend reviewing, for each pending or prospective claim, the strength of the evidence available on how income and tax credits were passed through to investors, so that claims are positioned to meet the standard the Supreme Court is likely to apply.

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