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Volume 8

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Volume 8

Taxation of Intercompany Dividends under Tax Treaties and EU Law

and achieve uniformity in the allocation of taxing rights between countries in cross-border situations.

overlap of different tax systems, and in particular

Tax Law

The main international sources of tax law are bilateral or multilateral treaties and on important source for the inter countries involved.

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Chapter 17: Italy

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17.1. The meaning of “dividend” under domestic non-tax law

No definition of “dividend” is embodied in Italian non-tax law. According to the literature, dividends are the fruit of the participation of the shareholder in the capital of the company. [2]

In Italian corporate law, the term “dividend” is used in the Civil Code (*Codice Civile*, “CC”) in connection with corporate legal forms (*società di capitali*). The basic rule is stated in Art. 2433, headed “Distribution of profits to the shareholders”, as amended by the 2003 corporate reform, [3] according to which a shareholders’ resolution is required for the declaration of dividends. Thus, the distribution of profits is approved by the shareholders’ meeting, which previously approves the financial accounts. [4] That is to say, a shareholders’ meeting may decide either to distribute the residual profits or to retain them for reinvestment. [5] If the shareholders’ meeting does not decide to distribute the profits, the shareholders are not entitled to receive dividends. It should be noted that “distribution of profits” pursuant to Art. 2433 does not necessarily correspond to a capital surplus and so to liquid assets: there may be profits – then distributable – even without cash assets. [6] Dividends cannot be paid except out of profits *actually obtained* and resulting from the regularly approved financial statements (Art. 2433(2)).

Based on the above, dividends may only be paid out of funds in excess of the company’s capital and legal reserves. [7] It must be pointed out that a 5% quota of the profit has to be set aside by law until such time as a legal reserve corresponding to 20% of the capital is set up (Art. 2430 CC).

If a loss of the company’s capital occurs, the distribution of profits cannot be made until the capital is replenished or reduced in a corresponding amount (Art. 2433(3) CC). Lastly, dividends paid in violation of the provisions of Art. 2433 CC cannot be claimed back if the shareholders collected them in good faith on the basis of regularly approved financial statements, from which corresponding net profits resulted.

Dividends are usually paid in cash. However, they may be paid in the form of stock or property (in-kind distributions). Thus, all operating expenses being met, the dividend policy’s most important use could be considered to return excess cash to the shareholders as well as to manage the company’s cash needs and capital structure.

Since before the 2003 reform, the Civil Code has granted the option to pay interim dividends. Art. 2433*bis*, indeed, allows such payments in advance of the dividends before the approval of the balance sheet provided the following requirements are met:

- the corporate by-laws allow such payments of interim dividends;
- the financial statements are, by law, audited by registered independent auditors;
- the independent auditors have approved the balance sheet of the previous accounting period; and
- the approved financial statements do not report losses for the previous year or for prior years.

The payment of interim dividends must be approved by the board of directors on the basis of the financial statements and of a report showing that the company’s financial position, results of operations and cash flows allow such payment. An opinion of the independent auditors concerning the above has to be obtained. Finally, if the intended profits are not realized, the interim payment has to be repaid to the distributing company, unless the shareholders prove their good faith.

The above-mentioned article of the Civil Code also requires, at Art. 2433*bis*(4), that the amount of the interim dividends does not exceed the lower of the amount of the net profit earned since the end of the previous accounting, net of any amounts that must be allocated to the reserves pursuant to the law or the by-laws, and the amount of the available reserves.

Pursuant to Art. 2433*bis*(6), the financial statements, the directors’ report and the independent auditors’ opinion must be deposited at the company’s premises until the balance sheet is approved so that the shareholders can examine it.

Dividends have to be booked in accordance with the principle of accrual basis accounting. [8] Such principle defines the moment from which the right for shareholders to claim dividend distribution arises.

As regards silent partnerships (*contratti di associazione in partecipazione*) under company law, Art. 2549 CC defines them as the agreement according to which the partner agrees to share the profits of its enterprise or of one or more businesses against the contribution made by the silent partner (which may be in cash, in-kind or in the form of works and services). Absent a different agreement, the silent partner also

participates in the losses of the enterprise *pro quota*, within the limits of its contribution. [9]

Profit sharing agreements (*contratti di cointeressenza*) are subject to similar rules. In accordance with Art. 2554 CC, such agreements may consist in:

- the participation of the associated partner in the profits and losses of the enterprise, without any kind of contribution (*cointeressenza propria*); or
- the participation of the associated partner in the profits of the enterprise, but not in the losses; in this case the associated partner would have to make a contribution in the enterprise (*cointeressenza impropria*). [10]

In addition to the traditional means of corporate financing, the 2003 reform of Italian corporate law introduced new possibilities, widening the applicable rules concerning shares and other financial instruments through which the companies organized in the form of a joint-stock company (*società per azioni*, "S.p.A") and of a limited liability company (*società a responsabilità limitata*, "S.r.l.") can raise risk capital and debt capital.

Thus, the reform has widely amended the existing provisions of the Civil Code of 1942, according to which the financing means had to come directly from the shareholders or through self-financing, or loans and other forms of debt capital, such as bonds. Such system has resisted innovations until Italian companies started to compete with foreign enterprises on a wider, Continental, market. The result of the 2003 corporate law reform is that the traditional distinction between equity and capital is fading.

The core innovation of the 2003 reform consists in the possibility to vary the content of the financial instruments according to the needs of the company. For instance, Art. 2411.2 CC now explicitly states that bonds can be issued with a right to participate in the economic performance of the company. Also, the repayment of the capital can be subordinated to the satisfaction of other debts. [11]

Also, the category of profit participating securities other than shares (Art. 2346.6 CC) was regulated. Hybrid financing has therefore been acknowledged in the Civil Code.

Hybrid financial instruments are characterized by features at the same time common to shares and debt instruments. [12] The basic features of such "hybrid instruments" have been borrowed from those legal systems where they were already known.

In the common law literature, "a hybrid security is so called because it combines some features of a debt security with some features of an equity security". [13] Although with different meaning, the use of the term "hybrid instruments" (*strumenti ibridi*, *hybride Finanzierungsinstrumente*, *valeurs mobilières hybrides*) is quite common in the literature of different countries.

As emerges from a comparative analysis, the elements that can make debt instruments similar to risk-bearing bonds consist in:

- the direct and reverse convertibility of bonds into shares (direct and reverse convertible bonds);
- the participation of bonds in the distribution of profits (profit participating bonds);
- the deferral of the payment of interest until the maturity date (zero coupon bonds);
- the subordination of the repayment of the borrowed capital (subordinated bonds);
- the postponement in the participation to the losses of the company; and
- the absence of a maturity date (perpetual notes).

Vice versa, the characteristics that may fade the nature of equity into that of debt are:

- the absence of a participation into the full profits of the issuer (non-participating preferred stock); and
- the possibility to redeem the shares at a given maturity date, either at the option of the shareholder or at the option of the issuer (redeemable stock).

In order to stress the relevance of a phenomenon which has long not been taken into due consideration in Italy (at least until the last financial crisis and the consequent need of financial companies to raise fresh capital), it has been noticed that in countries such as Germany and the United States, around 20% and 25% respectively of the "equity" employed by corporations is hybrid in nature.

The traditional distinction between equity and debt, although still existent and of utmost importance (in particular for accounting and tax purposes), has therefore blurred and will likely do so more and more as markets and governments develop their strategy out of the recession. [14]

Also, the corporate law reform introduced the possibility for a corporation to constitute a separate line of business endowed with its own equity and enjoying the limitation of liability into which third parties may take up the role of shareholders (Art. 2447ter CC).

All these innovations brought the literature to state that the traditional distinction between equity and debt is fading, so that there might be bonds which actually participate more than some kind of shares (e.g. preferred shares or saving shares) in the economic performance of the company and shares that enjoy

greater protection of the investment compared to those provided to certain profit-participating bonds. The main distinction between debt and equity can therefore no longer be seen in the degree of participation in the entrepreneurial risk.

While shares and profit participating securities issued under Arts. 2346.6 and 2447*ter* of the Civil Code can be classified as "participating" securities because they always entail a participation in the corporation (although not always in the form of a quota of the share capital), bonds and other non-participating securities are characterized by being based on an agreement between the company itself and the bondholders, [15] regardless of the degree of participation in the economic performance of the company (which as said above might be even higher, in certain cases, than that of some "participating" securities). The term "participation" is thus used more with reference to the nature of the securities and the corporate rights that they entail, rather than with reference to the character of their remuneration.

The above-mentioned 2003 reform of corporate law therefore brought with it a need to update the tax treatment of financial instruments, and hence the reform of the corporate income tax (*imposta sul reddito delle società*, hereinafter, IRES) introduced via Legislative Decree 12 December 2003, No. 344, then amended by Legislative Decree 19 November 2005, No. 247 and by Law Decree 4 July 2006, No. 223, converted into Law 4 August 2006, No. 248.

17.2. The meaning of "dividend" under domestic tax law

For IRES (i.e. corporate income tax) purposes, dividends consist in "profits derived from the participation to the share capital or equity of companies and entities which are subject to the corporate income tax" (Art. 44(1)(e) of the Income Tax Act, *Testo Unico delle Imposte sui Redditi*, Tuir (Presidential decree 22 December 1986, No. 917), hereinafter ITA). Income not deriving from such a participation will not be treated as dividends *stricto sensu* (except as what we will see below). Income deriving from the participation in partnerships is taxed on a flow-through basis and therefore not treated as a dividend. [16]

In this respect, the Italian Tax Agency stated that "such a conclusion is confirmed by Art. 44(1)(f) ITA, which distinguishes income derived from a silent partnership agreement from dividends". [17]

Despite the distinction in the definition of dividends and items of income deriving from the acquisition of other securities and from the participation in a silent partnership, under some conditions, Italian tax law provides for a treatment of these items of income for the most part in common to the tax treatment of dividends.

According to the government report that accompanied the tax law reform,

[T]he reference to the participation in the share capital or the equity of the company contained in Art. 44(1)(e) of the Income Tax Act and the definition of "financial instruments similar to shares" matches the new possibilities in the issuance of financial instruments following the corporate law reform of 2003, inclusive of those instruments which give right to participate in the profits of a given separate business of the company under Art. 2447*ter* of the Civil Code, when the financing third party takes up the role of a shareholder in the said separate business of the company.

Profit participating bonds regulated under Book V, Title V, of the Civil Code such as:

- profit participating bonds giving some administrative and economic rights to the holder, with the exclusion of the right to vote in the general shareholders' meeting, also when issued in consideration of the provision of works and services under Art. 2346 CC; [18]
- bonds issued in consideration of the contribution of assets into the separate lines of business set up by the company under Art. 2447*ter*(1)(e) CC; and
- other financial instruments which, regardless of their formal definition, condition the date and amount of the restitution of the capital invested to the economic performance of the company (Art. 2411(3) CC),

do not give rise to dividends in the proper sense of the term under Italian tax law. The tax treatment of such income, however, under certain conditions, is made equal to that of dividends through Art. 44(2)(a) ITA, which provides the definition of "financial instruments similar to shares".

These instruments are those "issued by a corporation or a commercial entity subject to the corporate income tax carrying the right to a remuneration which is fully linked to the economic performance of the issuer or of a company of the same group of the issuer or of a separate line of business in relation to which the securities were issued". [19]

The equalization of the tax treatment of these instruments to that of dividends is granted only in case of securitization: silent partnerships are excluded from such an assimilation, although their treatment is ultimately equal under many aspects (see below).

The assimilation to shares is not much linked to the risk borne by the subscriber of the above-mentioned financial instruments, but rather to the remuneration carried by the securities. Such criterion corresponds

to the anti-avoidance ratio that led to the introduction of Art. 109(9) ITA, according to which "no deduction shall be taken for the remuneration directly or indirectly paid in connection with: a) securities named under Art. 44 ITA for the part of their remuneration linked to the economic performance of the issuer, of a company of the same group of the issuer or of the separate line of business in connection with which the securities were issued".

With a separate provision, the same rule is provided with respect to income from a silent partnership (or from a profit-sharing agreement/*contratto di cointeressenza*) where the silent partner provides it with a contribution other than in the form of works and services (mixed contributions of capital on the one hand and works and services on the other do not bar the deduction of the remuneration).

The exclusion of the deductibility is limited to the remuneration of the bonds mentioned under Art. 44 ITA and therefore does not apply in case of derivatives or other financial instruments not mentioned under the same provision (but rather under Art. 67 ITA), regardless of the fact that the latter instruments may give right to a share of the profits of the issuing entity or of a company of the same group.

As the denial of deductibility follows the direct or indirect participation in the profits, it will make no difference whether the security also carries a share in the losses. Also, in the case of securitized financial instruments, the deduction will be denied regardless of the nature of the contribution in the company, i.e. regardless of the fact that such contribution be of capital or of works and services. [20] This draws a difference compared to the treatment of a silent partnership, since in this case, if the silent partner contributes works and services, the enterprise will be allowed deduction of the remuneration. [21]

With respect to securities, the government report accompanying Legislative Decree 344/2003 stated that the denial of deduction does not cover income which is linked to the performance of the enterprise only in that the payment is conditioned upon the company making a certain performance (in the Latin used by the government report, *an*), without however conditioning the amount of the payment upon the amount of profits (*quantum*), as in the case of bonds with a given rate of return. This means that the payment of interest conditioned upon the mere existence of profits or upon the actual distribution of dividends by the issuing entity or another entity of the group will be deductible; in such cases, indeed, there will be no sharing whatsoever in the profits of the enterprise.

On the basis of this reasoning, the Tax Agency has clarified that bonds and other unredeemable securities issued by banks under Art. 12 of the Italian banking law [22] do not suffer the denial of deduction on their remuneration. This is because such remuneration is not linked in its "*quantum*" to the profits of the bank, but rather only for its "*an*". In fact, the remuneration of such securities is usually fixed or linked to a floating interest rate, while the provision under which such securities may under certain circumstances participate in the losses of the bank does not mean that their holders take advantage of the economic performance of the company (i.e. have a share in the profits). [23]

The denial of deduction is directly dependent on the degree of participation of the securities in the profits. Therefore, securities only partially participating in the profits of the enterprise will suffer only a partial denial of deduction on their remuneration.

With a partial deviation from symmetry, as said above, the remuneration of the securities can be taxed as dividends only in case it is *fully* linked to the profits of the enterprise, and this may lead to unresolved economic double taxation by lack of integration of the taxation of the holder and of the issuer.

An interesting case concerning the debt/equity distinction for Italian tax purposes arose with the introduction of the "special bank bonds" [24] regulated under Art. 12 of Law decree 185/2008, converted into Law 28 January 2009, No. 2 (so-called "Tremonti bonds"). [25] The purpose of these securities is to increase the core capital of listed banks so as to help them out of the financial crisis and favour the access of enterprises to bank credit. The main characteristics of Tremonti bonds are the following:

- (1) they are non-voting securities (Art. 2436(6) CC) as they are denied the voting rights provided under Art. 2351 CC;
- (2) they shall be accounted in the core tier 1 capital of the bank (or for that matter of the banking group);
- (3) they do not carry a right of reimbursement of the capital; the reimbursement or the redemption are at discretion of the bank, under prior approval of the Bank of Italy having regard to the solvability and financial strength of the issuer; otherwise, the reimbursement will take place upon the liquidation of the bank;
- (4) they are subordinated, in the sense that their repayment will be made only after all other debts have been satisfied;
- (5) their remuneration is linked to the distributable profits of the bank, although it can never exceed 15% of the face value of the bond; the remuneration will be deducted from the distributable profits and cannot exceed their amount; in addition, the remuneration will be equal, subject to above-mentioned conditions, to the higher of:
 - (a) a minimum interest rate (increasing over time and starting at 7.5%), or
 - (b) 105% of the dividends actually distributed by the bank, or
 - (c) as of the tax period 2011, an amount linked to the long-term (30 years) treasury bonds;

- (d) the remuneration is not cumulative; namely, the amounts that are not paid to the holder in a given year are foregone;
- (6) they participate in the losses of the bank at the same degree of the ordinary shares, both in case of bankruptcy and in case of losses that produce a decrease of the core tier 1 capital below the regulatory threshold of 8%;
- (7) under certain conditions provided by law, they are convertible into ordinary shares at the option of the issuer (i.e. they are reverse-convertible);
- (8) the authority to approve their issuance is attributed to the board of directors, as in the case of debt bonds; and
- (9) they cannot be transferred without the approval of the issuer.

The absence of an obligation to reimburse the capital is the main proof of the character of the securities as non-debt securities, as this characteristic is required by Art. 44(2)(c) ITA for the qualification of a financial instrument as debt for tax purposes (together with the absence of a direct or indirect participation in the management of the issuer or of a control over such management).

Rather, these securities show a closer resemblance with equity instruments, as they carry a right to share in the distributable profits of the bank (i.e. their remuneration is not simply indexed upon such profits). All these characteristics led the Bank of Italy, CONSOB and ISVAP [26] to release a joint document [27] in which they stipulated instructions regarding the correct accounting of Tremonti bonds among equity instruments. For tax purposes, the main stream of the literature supports the characterization of Tremonti bonds as equity instruments, and not debt, [28] based on the link of the remuneration of these securities to the economic performance of the issuing bank, both for the "*an*" [29] and for the "*quantum*". [30]

In this context, in order to bring more certainty, Art. 2(22) of Law decree 138/2011, has finally stated that all financial instruments issued by companies under the controlling authority of the Bank of Italy and ISVAP in order to strengthen their core tier 1 capital and different from shares and similar instruments will be treated as bonds under Legislative decree 239/1996, and their remuneration will be deductible with the only limits set by Arts. 96 and 109(9) ITA.

17.2.1. The Italian tax treatment of inbound dividends

Before being reformed in 2005, the Italian tax system considered as inbound dividends, and therefore taxed it accordingly, only income flowing from a participation in the share capital or equity of the foreign company that, if paid by an Italian company, would have been fully non-deductible under Art. 109(9) ITA.

This meant that income not directly linked, both for the "*an*" and for the "*quantum*", to the economic performance of the enterprise was not treated like a dividend: securities bearing a remuneration linked to a given interest rate, for example, were not treated like shares, the income of which should be taxed like a dividend. Profit-participating bonds, which by definition do not bear a stock of the share capital nor of the equity, could not be treated like dividends, regardless of their treatment in the foreign state (i.e. regardless of the fact that their remuneration is deductible or not for the issuer).

As thereafter clarified by the Tax Agency, [31] such treatment was based on the presumption that the remuneration of securities participating in the share capital or in the equity of the enterprise was not allowed deduction in the foreign state, while the opposite was believed for other securities.

The rationale of such treatment was to reduce the risk of international tax arbitrage based on the different regulation of the remuneration in the state of the issuing entity and in the state of the holder, whereby in particular a deduction can be taken in the former and an exclusion or exemption in the latter with respect to the same item of income. Other countries, like Germany, have taken a different approach to this issue and introduced in some of their treaties a switch-over clause under which, in case of deduction of the remuneration in the foreign state, the flow of income will undergo full taxation in Germany, regardless of its characterization as a dividend. [32]

As mentioned above, as of 1 January 2006, the Italian system has been reformed and now provides for an equalization of foreign securities to Italian stock in case the remuneration is fully non-deductible for the issuing entity. Such non-deductibility must be confirmed by the issuing entity itself or result from other reliable documentation. [33] The reform also aimed at preventing possible infraction procedures under EU law.

The government report to this latter reform clarified that it thereby intended to eliminate any kind of discrimination against foreign securities when their remuneration is fully linked to the economic performance of the issuing entity and fully non-deductible. In case the foreign stock cannot be treated like shares, the tax treatment of debt securities or atypical bonds will apply.

Therefore, the rules actually in force do not require that the foreign securities entail a participation in the share capital or in the equity of the issuing entity, but rather consider sufficient for the sake of the equalization to Italian stock for tax purposes that their remuneration be treated like a dividend in the

foreign state, and thus denied deduction (beside being fully linked to the economic performance of the enterprise).

Absent the conditions for the equalization under the Italian tax regime, a foreign security will not be granted the treatment of shares, regardless of its qualification in the source state. For example, securities whose remuneration was treated like a dividend in the source state, but that did not carry a full link to the profits of the enterprise, could not be treated like a dividend for Italian tax purposes. This would remain unchanged even in case of application of a double tax convention designed according to the OECD Model Convention. Indeed, Arts. 10(3) and 23 of the OECD Model compel the residence state to grant a credit (or an exemption for those countries adopting a territorial approach in international taxation) for the foreign withholding taxes, but do not force it to treat the payment as a dividend for its own tax purposes.

Under certain circumstances, it is debatable whether inbound income that is treated as a dividend in the foreign state can also enjoy the treatment of dividends in the state of the holder of the security. In case of the German *Ausgleichzahlung*, for example, Italy should most likely recognize the treatment of dividends to these payments, as they in fact substitute a dividend. [34]

17.2.2. The Italian tax treatment of dividends and comparable items of income

Having defined what is a dividend and what items of income enjoy the same treatment of dividends for Italian tax purposes, we can now describe their taxation under Italian rules. [35]

As of 1 January 2004, Italy swept away its old-fashioned and EU-despicable imputation system and introduced a participation exemption regime for the taxation of capital gains on the sale of shares and comparable securities. This also brought with it a change in the tax treatment of dividends and comparable income, which now only partially undergo taxation. The specific rules for the taxation of dividends "and the like" income differ according to the characteristics of the holder of the securities (or, for that matter, of the silent partner in case of silent partnership agreements).

Dividends received by an individual holding qualified stock in a company outside its business activity are included in its taxable income in the amount of 49.72% (i.e. 50.28% of the dividend is excluded from taxation). [36] Qualified stock is defined under Art. 67(1)(c) ITA as stock representing a share higher than:

- 2% or 20% of the voting rights in the general shareholders' meeting; or
- 5% or 25% of the share capital or equity of the issuing entity, depending on the company being listed or not.

Dividends from unqualified stock, on the contrary, need not be reported in the annual tax return if they are received outside a business activity, as they suffer a substitutive tax of 12.5%, usually applied in the form of a final withholding tax by the withholding agent. [37] The rate of 12.5% will be increased to 20% as of 1 January 2012. [38]

Art. 47.1 ITA also provides for an irrebuttable presumption according to which profits and reserves of profits are always considered to be distributed before other taxed reserves, regardless of the corporate statements. As long as a company has profit reserves, therefore, tax-wise it will be considered as having distributed them, regardless of the fact that a restitution of the share capital was formally approved.

The same treatment provided for dividends, as mentioned above, is provided for silent partnerships, in that qualified participations of the silent partner bring a partial exclusion of the remuneration in the same amount of the dividends (i.e. 50.28%). A qualified participation in these cases is considered to be that above 5% or 25% of the equity of the enterprise as reported in the most recent balance sheet before the signature of the silent partnership agreement, depending whether it is listed or not. In case of unqualified participations, once again, the treatment is the same as for dividends (i.e. the 12.5% substitutive tax applies).

The above also holds true in relation to securities that are compared tax-wise to the shares as per the rules described above. When they represent a share in the equity, their characterization as qualified or unqualified participations will be measured based on the participation in the equity of the enterprise (higher of respectively 5% or 25%). [39] The participation in the equity of the enterprise has to be interpreted as a right to recover the capital contributed. [40] Securities not representing a share in the equity of the enterprise are always treated as qualified stock. [41]

Art. 47(5) ITA states that the distribution of reserves of capital or other provisions constituted with share premiums or contributions by the shareholders are not to be treated as distributions of dividends. Rather, such distributions reduce the cost basis of the securities of the shareholder. Stock dividends are not taxable, [42] nor are increases of the share capital through the use of profit reserves.

Dividends are taxed on a cash basis [43] and it is irrelevant whether the recipient of the payment was not the shareholder at the time the distribution was approved. [44] In the past, the Ministry of Finance has taken a questionable position according to which the surrender of a credit for the payment of the approved

dividends should be seen as treated as a constructive payment of the dividends to the shareholder and subsequent contribution of the same amount in the company. [45] Note, however, that case law took a position against such constructive taxation. [46] According to a recent decision of the Supreme Court, [47] uncollected amounts of dividends should be considered as loans granted by the shareholders to the company, thereby resulting in the taxation of interest on a presumptive basis. [48]

However, if the increase was made with reserves other than capital reserves, reserves for share premiums and the like, the successive reduction of the share capital will be treated as a distribution of profits. The reduction of the share capital will be imputed primarily to the reserves of profits that were used to increase it, from the most ancient one onwards, with the only exceptions provided by specific laws on the revaluation of reserves.

With reference to the redemption of shares, liquidation and reduction of the share capital, Art. 47(7) ITA states that any sum or value exceeding the cost basis in the hands of the shareholder will be treated as a dividend. This is because the income in question derives from the investment of capital, rather than from the realization of a capital gain, which is on the contrary the case when the shareholder leaves the company by way of a sale of his or her stock. [49]

With specific reference to foreign stock, after confirming the application of the general rules provided for domestic dividends and similar income, we shall recall that a material obstacle to direct portfolio investments in foreign companies is represented by the same substitutive tax mentioned above. Unqualified stock, in fact, produce dividends that are taxed via this substitutive tax and do not concur to the formation of the taxable income of the holder of the securities. Such an exclusion from the general taxable income brings with it a denial of any credit for the taxes eventually suffered in the source country. [50] Notwithstanding protests and criticism by the literature and the EU Commission, [51] the current structure might resist possible challenges before the ECJ, should the latter not change (or better draft) the principles laid down in *Kerckhaert-Morres* and then confirmed in *Damseaux*. [52] The substitutive tax of 12.5% is applied on the amounts cashed by the resident holder of the securities net of the foreign withholding tax. [53]

In case of qualified stock, on the contrary, dividends undergo ordinary taxation, but the partial exclusion of 50.28% produces an equivalent curtailment in the amount of the foreign taxes that enjoy the foreign tax credit. [54]

Dividends and comparable income received by non-commercial partnerships (e.g. *società semplici*) are always taxed on 49.72% of their amount and never enjoy the 12.5% taxation of the substitutive tax.

Dividends received in the conduct of a business are taxed as business income and therefore do not benefit of the substitutive taxation, regardless of the percentage of holding. However, they always benefit of a partial exclusion from taxation, which varies from 95% (in case the shareholder be an entity subject to the corporate tax) [55] to 50.28% (in case of individuals and partnerships). Such partial exclusion is unconditional.

The exclusion also extends to the remuneration of silent partnerships where the contribution of the silent partner does not consist in works and services. The exclusion covers the distribution of dividends during the lifetime of the company as well as the distribution of reserves other than the reserves of capital upon the redemption of the shares, the reduction of the capital, the liquidation of the company or the exclusion of the shareholder, regardless of such distributions being in cash or in kind.

In case of blacklist dividends, the partial exclusion of dividends and similar items of income provided for individual businessmen, partnerships, non-commercial entities and corporate entities does not apply, unless the profits were already attributed to the Italian shareholder based on the CFC regime or a waiver of the CFC regime was obtained under Art. 167(5)(b) ITA (i.e. the profits were adequately taxed abroad).

Distributions received by corporate shareholders must be distinguished from those received by non-entrepreneurial taxpayers subject to the individual income tax. In the latter case, sums received upon the withdrawal, redemption, exclusion, reduction of the share capital or liquidation of the company are always treated as dividends for the part exceeding their cost basis. In the case of corporate shareholders, on the contrary, it is necessary to distinguish between sums deriving from reserves of capital and the like and sums deriving from other reserves.

For example, in case a corporate shareholder had a cost basis on the shares of 3,000 and received a sum of 4,500 upon the liquidation of the company, 4,000 of which deriving from reserves of capital, it would undergo taxation of capital gains (benefiting or not of the PEX regime) for the difference between 4,000 and 3,000, thus 1,000. The rest of its gain (500) would be treated as a dividend.

Dividends paid to non-residents suffer in principle a final withholding tax of 27%. [56] The levy is 12.5% in case of dividends from savings shares.

The withholding tax on outbound payments of dividends and similar income is reduced to zero if the EU

Parent-Subsidiary Directive applies ^[57] or to applicable rate provided by a bilateral convention when the latter applies.

The discrimination of foreign shareholders who could not claim the application of the Parent-Subsidiary Directive was the target of an infraction proceeding started by the European Commission in 2006, which finally brought to the conviction of the Italian regime by the ECJ. ^[58] Meanwhile, the Finance Act for 2008 had already reformed the withholding tax on outbound payments of dividends and similar income, so as to comply with EU principles. Based on the new Art. 27(3ter) of Presidential decree 600/1973, distribution of dividends and similar income to entities which are subject to the corporate tax in their country of residence within the EU or the EESA are subject to a withholding tax of 1.375%, which is equivalent to the taxation of 95% of the dividends under the nominal rate of the Italian corporate tax (27.5%). ^[59] The Tax Agency has recently provided for additional instructions in this respect. ^[60]

While there is no case law on the taxation of constructive dividends arising from a transfer pricing adjustment, the following can be said.

A transfer pricing adjustment of the profits of a subsidiary brings as a consequence an increase in its income for tax purposes. The adjusted income, however, was never at the disposal of the subsidiary, as it was directly earned by the foreign associated enterprise. In case the foreign associated enterprise were the controlling entity of the Italian subsidiary, a constructive dividend could thus be recognized, in theory. Such a result could be based on the case law of the Supreme Court regarding privately held companies. In such cases, when the income of these companies is reassessed by the tax administration it is common for the public officers to also assess the distribution of hidden profits to the shareholders. ^[61] While such an assessment cannot always be done (e.g. in case of a denial of costs actually incurred, but tax(wise non-deductible) one may argue that this line of reasoning, which goes under the name of secondary adjustments, ^[62] could also be applied in certain transfer pricing adjustments. Once again, the potential application of the Parent-Subsidiary Directive to the benefit of the foreign entity could make the reassessment pointless. It would be more debatable whether the same reasoning could support a reassessment in case of a transfer pricing adjustment of a transaction between sister companies. At the moment, as noted above, there are no precedents in Italian case law, nor in the instructions of the tax administration. ^[63]

Dividend washing and dividend stripping schemes have always been attacked by the Italian tax administration and finally declared unlawful by the legislator. ^[64] The Supreme Court initially confirmed the reassessments by the tax administration based on the *fraus legis* doctrine and the abuse of law as deriving from EU principles. After this rationale was fiercely criticized by commentators, the Supreme Court then moved to a different rationale, with the same result of confirming the reassessments. In these more recent cases, the Supreme Court upheld the reassessments based on the abuse of law doctrine as derived directly from Italian constitutional principles of equality and ability to pay. ^[65]

In the meantime, specific provisions were added to the code in order to counter dividend washing and stripping schemes. Under Art. 109(3bis) ITA et seq., capital losses on stock and similar instruments that do not fall under the participation exemption regime (and that are therefore entirely deductible) cannot be deducted for an amount equal to the distributions that were received from those securities in the preceding 36 months and that benefited from the 95% exclusion. As the rationale for such a denial is anti-avoidance, the provision only applies to securities that were acquired in the 36-month period before their sale (i.e. only to short-term – and indeed medium-term – participations). An exception is granted in case of IAS adopters, as in this case, the rules on taxation of dividends from short-term participations automatically impede dividend washing or stripping schemes. ^[66]

Other hypotheses of constructive dividend taxation might be seen in cases where the taxpayer benefited of an optional fiscal step-up of the cost basis of the shares under special revaluation provisions that the government has from time to time introduced in past years at the cost of the payment of a substitutive tax: in some of these cases, after taking advantage of the step-up the taxpayer sold its shares to associated taxpayers (frequently, a holding company controlled by the same subject), which thereafter paid the price of the sale in instalments that reflected the distribution of profits by the company whose shares had been sold.

Other cases, however, concern the recharacterization as dividends of loans granted by the company to its own shareholders, as a way to defer taxation while already putting the money at their disposal. ^[67]

In case of repo transactions, dividends received by the cash purchaser of the stock are taxable in its hands as such (i.e. not as the remuneration of a loan). ^[68] Art. 2(3) of Legislative decree 461/1997, however, denies the 95% exclusion, as well as the credit for foreign taxes in case the cash seller could not benefit of the 95% exclusion or of the foreign tax credit. While objections based on the violation of non-discrimination under tax treaties and EU law may arise, the literature considers such a provision applicable to all cross-border repo transactions. ^[69]

17.2.3. The treatment of dividends and similar income in case of IAS adopters

As of 2005, Italy has introduced a particular regime for companies adopting the International Accounting Standards (IAS-IFRS). After a number of policy changes, the current regime confers relevance for tax purposes to the income as determined under the IAS/IFRS. This statement of principle is valid with reference to the characterization, classification and imputation of income, [70] but there are a number of exceptions and detailed rules. [71]

With respect to dividends, a basic distinction has been drawn between shares that are "held for trading" and other shares. [72] The latter are indeed treated as long-term investment and therefore benefit from the participation exemption regime for capital gains taxation purposes. The former, as short-term investments, do not benefit of the PEX regime. This is reflected also in the taxation of dividends, as those deriving from shares that are held for trading do not benefit of the 95% exclusion from taxation. [73] Such a rule is meant to match with the full relevance of valuations of the shares that are held for trading. Every time a dividend is received, the shares that are paying it decrease in value for a corresponding amount and such decrease, as reflected in the accounts under the IAS/IFRS, is fiscally relevant. [74]

After some discussions in the literature [75] on whether the distinction between shares and similar securities and bonds and similar securities drawn by Art. 44 ITA was to be maintained also with respect to IAS adopters, [76] Art. 5 of Ministerial decree of 8 June 2011 has finally overcome the uncertainty and – with the declared goal of avoiding double taxation or non-taxation and achieving a symmetric treatment for the issuer and the holder of the securities, regardless of their nature – stated that in this respect IAS adopters should follow the same rules provided for all taxpayers. [77]

This can trigger a difference in the accounting and tax treatment of a single security, which, for example, could be treated as equity for accounting purposes and as a bond for tax purposes, with the consequence that its remuneration would not be deductible tax-wise.

17.3. Tax treatment of dividend distributions under special tax regimes in domestic law

Italian tax law provides certain special regimes that affect the treatment of dividends.

The first of these is the consolidation regime, which can be domestic [78] or worldwide. [79] These regimes were introduced based on Art. 4 of Law 80/2003, which also imposed the denial of the deduction of unrealized losses deriving from the valuation of the shares in the subsidiaries. [80]

Under the domestic consolidation regime, a corporate taxpayer having control according to Art. 2359(1)(1) CC (i.e. majority of voting rights in the ordinary shareholders' meeting) over a resident subsidiary may elect, together with the latter, to consolidate its income/losses with those of the subsidiary(ies) for tax purposes. The option for the domestic consolidation can be made only if the controlling entity also has a right, directly or indirectly, to more than 50% of the profits made by the controlled entity(ies). Non-voting shares should be ignored for the sake of these requirements.

A foreign entity may also elect for the consolidation in the quality of consolidating entity, provided it resides in a treaty country and it conducts a business activity in the country through a permanent establishment to which the shares of the subsidiary(ies) are attributed.

The election is valid for 3 years and cannot be revoked. The consolidation is achieved by adding up the income and losses of the single consolidated companies, regardless of the percentage of participation by the controlling entity. In case of multiple layer groups, the percentage of control has to be decreased by multiplying the quota detained in the first-tier subsidiary (sub-holding) in the second-tier subsidiary and so on. This means that if company A holds 60% of the shares of company B, which holds 51% of the shares of company C, the latter will not be eligible for the consolidation regime of A (however, it could enter a consolidation regime with B). [81]

Sums paid as a compensation for the tax benefits deriving from the consolidation are fiscally irrelevant. [82]

Art. 1(33)(s) of Law 24 December 2007, No. 244 modified Art. 122 ITA and repealed the so-called tax consolidation adjustments that had to be made to the sum of the single income attributed to the fiscal unit by the consolidated entities. Among these adjustments there were also those regarding the distribution of intra-group dividends, which were irrelevant for tax purposes. The irrelevance concerned dividends paid during the consolidation regime, irrespective of the formation of the profits that gave origin to the distribution. Thus, distributions of profits realized by the subsidiary before the consolidation benefited from the complete exclusion of taxation when distributed to the shareholding company participating in the consolidation regime. On the other hand, dividends distributed after the expiration of the consolidation regime were taxable under the ordinary rules, regardless of the fact that the profits of subsidiary were

realized during the consolidation regime.

After the repeal, on the contrary, intra-group dividends, also within a consolidated group, follow the ordinary rules described above. The same can be said with regard to the regime of worldwide consolidation. [83]

Besides the rules on domestic and worldwide consolidation, the ITA also provides for an optional regime that can be applied to privately held companies under Art. 115 ("check-the-box" rules). For privately held companies in this context, this means companies whose shareholders are companies as well, which are also subject to the corporate income tax under Art. 73(1)(a) ITA and that hold quotas or shares between 10% and 50% of the voting rights and of the profits of the former. In these cases, an option can be made for having the profits of the participated company directly attributed on a look-through basis to the shareholders. [84]

Tracking shares and non-voting shares shall not be counted for the purposes of the application of the present regime. The option cannot be made if the shareholders benefit from a reduction of the corporate tax rate as well as if the company is part of a consolidation regime, be it domestic or worldwide, or enters bankruptcy proceedings. [85]

The option is also open to foreign shareholders, provided the outbound distributions of dividends by the company are not subject to withholding taxation. [86]

Tax credits and losses of the transparent company are attributed pro quota to its shareholders, although there are some limits to the attribution of losses. [87] The regime is valid for 3 years and cannot be revoked. The distribution of reserves of profits formed before the option was made or of reserves of capital and the like follows the ordinary rules. There is a rebuttable presumption [88] that during the validity of the regime of transparency distributions be made with profits attributed on a transparent basis to the shareholders. [89] The same reserves of profits are considered to be previously used when covering losses.

Under Art. 8 of Ministerial decree 23 April 2004, the distributions of profits attributed to the shareholders on a transparent basis do not undergo taxation, even if they take place after the expiration of the regime and in the hands of a different (i.e. new) shareholder, under the sole condition that the new shareholder meets the same requirement of corporate form provided under Art. 1(1) and (2) of the decree.

The cost basis in the shares of the transparent company is increased by the same amount of profits attributed on a transparent basis to the shareholders and correspondingly reduced by an amount equal to the losses attributed to the shareholders. Also, the cost basis is reduced for an amount equal to the dividends actually distributed by the check-the-box company. [90]

Similar rules are provided under Art. 116 ITA for limited liability companies (*società a responsabilità limitata*) with a turnover below the threshold provided for the application of the *studi di settore* (standard assessment of income) and whose capital is exclusively held by less than 10 individuals, or less than 20 in case of cooperatives.

The conversion of a partnership into a corporation subject to corporate income tax does not trigger the taxation of the distributions taking place after the conversion insofar as the profit reserves that were set up before the reorganization are inserted in the balance sheet of the corporation with a mention of their origin. [91] This is because doing otherwise would imply double taxing the same distributions, given that the income of a partnership is taxed on a look-through basis upon its shareholders, regardless of its actual distribution. [92]

In the opposite case of a corporation that converts into a partnership, reserves different from those of capital and the like are attributed to the partners as per Art. 5 ITA:

- (a) In the tax period of their distribution or use other than to cover losses, provided their origin is adequately reported in the balance sheet of the partnership;
- (b) In the tax period after the conversion takes place if no indication of their origin is reported in the balance sheet or if they are not inserted in the balance sheet of the partnership at all. [93]

The distribution of prior reserves by the partnership will be taxed under the rules for the taxation of corporate dividends, thereby maintaining the regime that would have applied on the distributions, had the conversion not taken place. [94]

Analogous rules are provided for the conversion of a corporation into a non-commercial entity [95].

The corporate tax reform of 2004 also brought with it the introduction of a tonnage tax regime, regulated under Arts. 155-161 ITA. Under this regime, Italian companies subject to the corporate tax under Art. 73(1)(a) ITA and foreign companies operating in the country through a permanent establishment may elect to be taxed under the special tonnage regime for a 10-year period in connection with income produced through the use of ships and vessels indicated under Art. 8bis(1)(a) of the VAT decree No. 633/1972 and

registered with the international registry under Law decree No. 457/1997. [96] The option has to be made with respect to all ships and vessels run by the parent company and its subsidiaries (i.e. companies controlled by the former as per Art. 2359 CC). The application of the tonnage tax regime rules out the regime of consolidation. [97] Income from the activities of carriage of goods and persons, sea-rescue, towage, realization and laying down of plants, instalments and facilities, as well as other activities of assistance to be executed offshore and other connected activities realized through the use of ships and vessels with a tonnage higher than 100 tons, is determined on a standard basis. [98] Income deriving from the leasing of the bare hull cannot benefit of the tonnage regime. [99]

The tonnage tax regime expires if the ships and vessels are not actively and directly used by the group above the thresholds stipulated by Art. 7 of the Ministerial decree.

Income deriving from activities other than those benefiting of the tonnage tax regime undergoes ordinary taxation. The tonnage tax is based on the standard determination of the taxable income upon which the ordinary tax rate is then applied, together with income produced from other sources, which, on the contrary, continues being determined on an analytical basis. [100] In the silence of the relevant provisions, this rule also applies to the dividends received by the companies that opted for the tonnage tax regime.

Art. 1(119) et seq. of the Finance Act 2007, [101] as modified by Art. 1(374) of the Finance Act 2008, [102] has introduced a special regime for listed companies who specialize in the real estate sector (*società di investimento immobiliare quotate*, SIIQ – real estate investment companies). [103]

These companies benefit of the exemption from the corporate tax and the business income tax of that portion of their income which is derived from the leasing of real estate. Income is only taxed upon its distribution in favour of a shareholder other than another SIIQ by way of a withholding tax of 20%, [104] which is final in case of private investors and similar taxpayers and creditable in case of entrepreneurial taxpayers. The withholding tax is applied by the intermediary that has the shares of the SIIQ in deposit, as the SIIQ would not be in a condition to identify its shareholders and thereby apply – or not apply – the levy. [105] Non-listed real estate investment companies (SIINQ), on the contrary, do operate as withholding agents in case their dividends are distributed to taxable shareholders. Dividends received by a SIIQ from another SIIQ or from a SIINQ (a non-listed real estate company who elected to benefit of the present regime together with its controlling and consolidating SIIQ) are also exempt. SIIQs are compelled by law to distribute at least 85% of their tax-exempt income on an annual basis. [106] While the activity of leasing of real estate has to be preponderant, as well as the value of the assets dedicated to such an activity, [107] a SIIQ may also conduct other minor business activities, the income of which will be taxed under the ordinary regime of business taxation. Latent gains on the real estate to be leased out have to be stepped up upon the election of the special regime: a substitutive tax may be applied in this case. The step-up is also reflected on the cost basis on the shares of the SIIQ held by the shareholders.

SIIQs are subject to the control of the Bank of Italy and CONSOB and undergo particular obligations with regard to the transparency of their activities and investment policies as well as with regard to the level of financial leverage they can incur.

No single shareholder may directly or indirectly hold more than 51% of the voting rights and of the profits of the SIIQ, while at least 35% of the capital has to be held by investors individually holding stock no higher than 2% (always in terms of both voting rights and profits). Investment funds, pension funds and public pension institutions may hold higher percentages of stock without thereby barring the possibility for the real estate investment company to benefit of the SIIQ regime.

Dividends deriving from the tax-exempt activities of the SIIQ cannot benefit of the Parent-Subsidiary Directive, as the subsidiary is not subject to tax in their respect. [108]

Dividends received by entrepreneurs and companies subject to business income taxation and deriving from tax-exempt profits of the SIIQ do not benefit of any kind of partial exclusion, as the rationale of the partial exclusion is to eliminate or lessen economic double taxation. Dividends received by investment funds, SICAVs, complementary pension schemes and individual asset management schemes are not subject to the withholding tax.

Capital gains on the sale of the shares of a SIIQ never benefit of the participation exemption. In order to adjust such a rule with the fact that a SIIQ may conduct minor activities which are subject to business income taxation it is provided that the cost basis of the shares be proportionally increased by the amount of taxable profits realized by the SIIQ and decreased by the amount of dividends received deriving from such activities. For the same reason, the cost basis also has to be increased by the amount of reserves of profits that incurred taxation in the tax period preceding the option to be treated as a SIIQ. Correspondingly, the distribution of these reserves will reduce the cost basis on the shares. By the same token, in case of expiration of the SIIQ regime the cost basis must be decreased by the amount of these reserves of taxed profits.

Italian resident investment funds (other than real estate investment funds) [109] are exempt from tax, which

is applied only on the distributions or realization of capital gains by the quota holders. On the contrary, foreign funds are subject to the ordinary withholding rates, which could ultimately result in a breach of EU law (see below for an analogous discussion concerning pension funds and the proceedings that were already opened by the EU Commission in this respect).

17.4. Dividend taxation for indirect tax purposes (VAT, transfer tax, etc.) and procedural issues relating to intercompany dividend taxation

17.4.1. Dividends and VAT and other indirect taxes

This section includes some considerations on dividends from the VAT perspective, starting from the question whether, and to what extent, dividends fall within the scope of the Italian VAT rules.

The starting point is the definition of a value added tax. According to EU Law, a VAT is a "general consumption tax" designed to be imposed on all commercial activities involved in the process of the production and distribution of goods and the provision of services (a general tax), and a tax to be borne by the final consumer (a consumption tax). [110] Consequently, activities that are not economic activities fall outside the scope of the tax. Under Art. 4(1) of the Sixth Directive, a taxable person is any person who independently carries out in any place any economic activity, which is defined as comprising all activity of producers, traders and persons supplying services and, inter alia, the exploitation of tangible or intangible property for the purposes of obtaining income on a continuing basis (Art. 4(2)).

That said, a number of judgments have been referred to the ECJ by national courts for guidance on the interpretation of the VAT rules related to shares and dividends. The Court has held that a holding company whose sole purpose is to acquire holdings in other undertakings, without directly or indirectly interfering in the management of those undertakings beyond the ordinary involvement as a shareholder, does not have the status of taxable person. Such conclusion is based on the fact that the mere acquisition of financial holdings in other companies does not constitute an economic activity within the meaning of the Sixth Directive, [111] but rather the mere exploitation of assets that does not create value added ("because any dividend yielded by that holding is merely the result of ownership of the property").

The first case that was brought to the attention of the ECJ in this respect was *Polysar*. [4] The ECJ specified the notion of "involvement", making it clear that in order to operate as a taxable person, a holding company has to carry out transactions that are subject to VAT by virtue of Art. 2 of the Directive, such as the provision of administrative, accounting, financial and commercial services to its subsidiary. [112]

It was also added that if the holding company is a taxable person in respect of the management activity for VAT purposes, dividends may be included in such an activity "only if" they may be deemed as a "consideration" for the services provided by the holding company, so assuming that there is a "direct link" between the mentioned activity (subject to VAT) and the consideration received. [113]

However, the receipt of dividends is not the consideration for any economic activity within the meaning of the VAT Directives, provided that they result from the mere ownership of the shares. [114]

In particular, the ECJ decisions, among others, in *Polysar*, [115] *F. and B.* [116] and *Cibo Participations* [117] pointed out that certain features of dividends account for their exclusion from VAT:

[F]irst, it is not in dispute that the existence of distributable profits is generally a prerequisite of paying a dividend and that payment is thus dependent on the company's year-end results. Second, the proportions in which the dividend is distributed are determined by reference to the type of shares held, in particular by reference to classes of shares, and not by reference to the identity of the owner of a particular shareholding. Lastly, dividends represent, by their very nature, the return on investment in a company and are merely the result of ownership of that property (*Polysar*, paragraph 13).

In view, specifically, of the fact that the amount of the dividend thus depends partly on unknown factors and that entitlement to dividends is merely a function of shareholding, the direct link between the dividend and a supply of services (even where the services are supplied by a shareholder who is paid dividends), which is necessary if the dividends are to constitute consideration for the services, does not exist. [118]

As a consequence, dividends resulting from shareholding fall outside the entitlement to deduction. [119] Thus, dividends must be excluded from the calculation of the deductible proportion referred to in Arts. 17 and 19 of the Sixth Directive, [120] "if the objective of the wholly neutral taxation ensured by the common system of VAT is not to be jeopardized". [121]

The ECJ case law on dividends and VAT is also supported by the Italian implementing provisions and by the literature.

As regards the Italian VAT rules, pursuant to Art. 1 of Presidential Decree No. 633 of 26 October 1972, [122] VAT is applied on the supply of goods and provision of services in the territory of the state in the conduct of a business, trade or professional activity and on imports carried out by anyone.

With respect to the notion of "economic activity", the lawmakers [123] have excluded from such notion the mere possession of assets for the sake of their exploitation. Art. 4(5)(b) of Presidential Decree No. 633/1972 indeed conforms to the EU case law mentioned above by stating that:

[T]he ownership, not instrumental or ancillary to other business activities, of holdings or shares and quotas, bonds and similar securities, held as fixed assets, in order to receive dividends, interest or other benefits, without structures designed to conduct financial activities, or steering activities, or activities of coordination or other forms of involvement in the management of subsidiaries shall not be considered as a business activity. [124]

The literature also agrees that dividends received do not affect the calculation of the pro rata of deduction. [125]

Once we recall the decision of the ECJ in *Cibo Participations*, we might wonder how to interpret the statement of the Court according to which:

[E]xpenditure incurred by a holding company in respect of the various services which it purchased in connection with the acquisition of a shareholding in a subsidiary forms part of its general costs and therefore has, in principle, a direct and immediate link with its business as a whole. Thus, if the holding company carries out both transactions in respect of which VAT is deductible and transactions in respect of which it is not, it follows from the first paragraph of Article 17(5) of the Sixth Directive that it may deduct only that proportion of the VAT which is attributable to the former.

In particular, one may wonder whether, irrespective of the amount and extent of taxable transactions realized by the holding company, all its input VAT should be deducted or not. According to Art. 19(2) of the Italian implementing decree No. 633/1972, in line with Art. 17(2) of the Sixth Directive, the deduction is granted only if the input VAT is linked to the taxable transactions of the taxpayer. [126] The issue may arise, for example, whether input VAT connected to the acquisition of services by the holding in order to improve the profitability of its investments through the subsidiaries that do not give rise to output taxable transactions (e.g., because the return of such an investment is represented by the increase in the amount of dividends received) shall be deductible or not. Based on *Cibo Participations* and *Floridienne and Berginvest*, such input VAT could be deducted as relating to the general activity of the holding company (let us assume the holding does not make VAT-exempt supplies). According to ruling No. 27/E of 29 January 2002 of the Tax Agency, the denial of the VAT credit does not apply insofar as the purchase of goods or services, although related to a non-VATable transaction, is indirectly linked to the realization of other taxable transactions. [127] This is a line of reasoning similar to the one adopted by the ECJ in *Kretztechnik AG*, [128] where the Court stated that input VAT related to advisory services received in connection with the issuance of shares in the context of an increase of capital (i.e. a non-VATable transaction) should be allowed as a credit provided the company performed wholly taxable activities which would then benefit of the capital increase. [129] A difference between *Cibo Participations* and *Kretztechnik*, however, is that in the former the taxpayer also received dividends (i.e. out of the scope income), while this did not happen in the latter case. [130] The ECJ decision in *Securenta* seems to lead to a conclusion different than *Cibo Participations*, in that the judges in the former case stated that input VAT linked to non-economic transactions (e.g. to the increase of the dividends to be received) cannot be deducted. [131]

While there is no specific case law in Italy in this respect, based on the characterization of the receipt of dividends as a "non-transaction" for VAT purposes, some authors have expressed the view that the deduction should be granted in full and irrespective of the dividends received, thereby escaping the limits imposed by Art. 19(2) and (4) of the implementing decree, at least as long as the output transactions are taxable in full. [132] Such a view, however, does not seem to be in accordance with the nature of the VAT as a consumption tax, which bars the deduction of inputs connected to the mere exploitation of goods through their possession, no different than in case of a private consumer who holds stock and asks for advice on how to best invest. More reasonably, the Ministry of Finance has to date clarified that input VAT can be deducted if it at least indirectly relates to the output taxable transactions. [133]

The characterization of silent partnerships (*contratti di associazione in partecipazione*) for VAT purposes has been an issue confronted by both the literature [134] and case law, [135] and which also led to official instructions by the Ministry of Finance [136] until 2003, when the government passed Art. 5(2bis) of Law decree 24 December 2002, No. 282, converted into law 21 February 2003, No. 27, which modified Art. 5 of the Italian implementing decree on VAT (Pres. Decree No. 633/1972). Up until that reform, it was debated whether or not the contribution by the silent partner should be subject to VAT (or for that matter, registration tax). The issue depended on the characterization of the silent partnership as an exchange

between the contribution on one hand and the participation into the profits of the enterprise on the other. The very letter of Art. 2549 CC expressly qualifies the return (the share into the profits of the enterprise) as the consideration for the contribution. The new provision makes clear that no VAT should be applied on the provision of services by the silent partner when such a provision is not connected to a VAT-relevant professional activity of the silent partner, thereby making the implicit assumption that VAT should ordinarily be applied on such contributions. [137]

17.4.1.1. The principle of the open market value in the VAT regime

In this respect, we should recall that the interest in transfer pricing adjustments for VAT purposes is relatively recent – since Directive 2006/112/EC – and it is still in an early stage of development. [138]

In order to contrast the price manipulation practices of intra-group transactions with the scope of abusing the asymmetries of the VAT regimes, there are some derogations to the general principle according to which the taxable amount for VAT purposes is determined by the contractual consideration. In such cases, the taxable amount is represented by the open market value of goods and services that are the object of the contract. The concept of “open market value” is defined by Art. 72 of Directive 2006/112/EC as “the full amount that, in order to obtain the goods or services in question at that time, a customer at the same marketing stage at which the supply of goods or services takes place, would have to pay, under conditions of fair competition, to a supplier at arm’s length within the territory of the Member State in which the supply is subject to tax.”

Art. 80 of the directive therefore allows Member States to assume as a taxable basis the open market value in respect of the supply of goods and services, instead of the consideration, when the latter is lower than the open market value and (i) the recipient of the supply does not have a full right of deduction, (ii) the supplier does not have a full right of deduction or (iii) where the consideration is higher than the open market value and the supplier does not have a full right of deduction.

Italy had originally reproduced such rules in Art. 1(261)(c) of Law 24 December 2007, No. 244 (Finance Act 2008), which replaced Art. 13(3) of Presidential Decree No. 633 of 1972 and introduced the relevance of the open market value for VAT purposes, initially only with reference to the taxable transactions made toward a subject who suffered a limitation on the right of deduction.

Thereafter, Law 7 July 2009, No. 88 reproduced in Art. 14 of Presidential Decree No. 633 of 1972 the definition of the open market value of Art. 72 of Directive 2006/112/EC, and thereby implemented the provisions of Art. 80(b) and (c), modifying the wording of Art. 13 of Presidential Decree No. 633 of 1972.

Therefore, the law as it actually stands in Italy is that the open market value applies instead of the consideration in the following cases of intra-group transactions: (i) for taxable transactions made at a consideration lower than the open market value toward a subject who has a limited right of deduction according to Art. 19(5) of Presidential Decree No. 633 of 1972; (ii) for exempt transactions made by a taxpayer with a limited right of deduction for a consideration lower than the open market value; and (iii) for taxable transactions with a consideration higher than the open market made by a subject who has a limited right of deduction according to Art. 19(5) of the same Decree.

The assignment of assets to the shareholders of companies of any kind or by other private or public entities, inclusive of those that are not incorporated, undergoes VAT if the purchase of the goods enjoyed a VAT credit. [139] Taxation is applied on the fair market value of the goods.

Apart from VAT, a lump sum of EUR 168 is due as registration tax (*imposta di registro*) with reference to distributions of cash [140] dividends or to distributions that are subject to VAT. [141] The distribution of immovable property undergoes proportional taxation for registration tax purposes according to the rates provided by the “Tariff” attached to the Registration Tax Act. The distribution of boats undergoes the application of the lump-sum tax (variable according to the dimensions of the boat) provided by Art. 7 of Part I of the Tariff; [142] the assignment of going concerns [143] and movable goods, as well as of other rights of any kind, undergoes taxation under the lump sum of EUR 168.

The capitalization of reserves is also subject to the lump-sum registration tax or at a proportional rate, depending on whether the reserve was subject to the tax at the time it was set up. [144] Thus, to avoid double taxation, when share premium reserves, tax-exempt monetary revaluation reserves or other non-refundable funds contributed by shareholders are capitalized, the registration tax is EUR 168. If other reserves are capitalized, it is 1% of the amount of the reserve. [145]

17.5. Selected issues in the tax treatment of cross-border inbound and outbound dividends under domestic law

17.5.1. Issues relating to entitlement to a foreign tax credit for inbound dividends

As discussed above, the Italian tax system provides for the elimination of economic double taxation by

excluding part of the dividends from taxation. The actual tax rates finally applied on individual shareholders are set so as to render the taxation of corporate profits analogous to the taxation of business income realized by individual entrepreneurs. [146]

With respect to inbound dividends, we shall recall the rule provided by Art. 165(10) ITA, under which income which is only partially subject to tax also brings a (only) partial credit for foreign taxes. This means that 95% of the excluded dividends will carry a correspondingly reduced foreign tax credit; the same applies for dividends incurring taxation for 49.72% of their amount. Dividends received by portfolio investors do not benefit of the foreign tax credit whatsoever, as they are taxed by way of the substitutive tax of 12.5% [147] under Art. 18 ITA [148] and cannot be included in the ordinary income to be declared in the tax return. The Italian levy applies on the net dividends distributed by the non-resident company (so-called "*netto-frontiera*" method). The levy of 12.50% is applied by the Italian intermediary (usually, a bank) intervening in the payment, but if the foreign dividends are directly received without the intervention of a resident intermediary, the Italian taxpayer must declare such dividends in his tax return and then apply the final levy (Art. 18 ITA). Under Art. 165(1) of ITA, which regulates the Italian foreign tax credit, however, it is not possible to benefit of a foreign tax credit if the foreign item of income is subject to an Italian final withholding tax. Therefore, in order to benefit from the foreign tax credit, the item of income of foreign source has to be included in the Italian aggregate taxable income of the taxpayer; and, as mentioned above, this is not the case of foreign dividends arising from foreign non-qualified participations received by Italian resident private individuals. Juridical double taxation thus arises and the bilateral conventions signed by Italy do not resolve the problem. For example, the convention with Germany currently in force states at Art. 24(2)(a) that

Subject to the provision of subparagraph (b) where a resident of Italy derives items of income which may be taxed in Germany, Italy, in determining its income taxes referred to in Article 2, may include such items of income in the taxable base upon which such taxes are imposed, unless specific provisions of this Convention provide otherwise. In such a case, Italy shall deduct from the taxes so determined the income tax paid in Germany; the deductible amount shall not, however, exceed that portion of the Italian tax which such items of income bear to the entire income. *Nevertheless, no deduction shall be granted if the item of income is subjected in Italy, according to the Italian law and upon request of the recipient of that income, to taxation by way of withholding at source.* (emphasis added)

While the letter of the provision may leave room for discussion when it requires that the Italian taxpayer actually requests being taxed by way of a final withholding, we shall stress once again that no such request is actually foreseen by the Italian tax system, which only provides for such final taxation outside of the aggregate taxable income to be declared in the tax return. In this respect, it should be added that this rule seems to be in violation of EU law [149] and, in particular, of the freedom of movement of capital granted under Art. 63 of the Treaty on the Functioning of the EU. Note, however, that the ECJ has excluded, to date, that such kind of restrictions can be considered as a violation of EU law. [150] The position of the EU Commission was that:

It is clear that the higher tax burden on inbound dividends constitutes a restriction in the sense of Article 56 of the EC Treaty on individual taxpayers to invest in foreign shares. Such a Member State may argue that it has a non-discriminatory system, which subjects both domestic and inbound dividends to the same tax treatment, and that the restriction is the result of the foreign withholding tax. However, this argument cannot be accepted if the Member State's relevant tax treaty gives the other State the right to levy a withholding tax (generally of 15%), and if Article 23 states that the Member State shall give a credit for this withholding tax. In such circumstances the restriction of the free movement of capital would be caused by the Member State itself, and not by the source State, as the OECD Model and the applicable tax treaties require that the residence State must provide the relief. [151]

The Commission recently issued a consultation paper in order to tackle this problem. [152]

17.5.2. Dividend taxation under CFC regimes

Italian CFC legislation provides for two different regimes regarding CFC companies.

The first concerns CFCs that are actually "controlled", [153] while the second concerns those companies resident in a tax haven (blacklist companies) in which an Italian resident directly or indirectly possesses qualified stock not amounting to control. [154]

In the first case, income of the CFC company is attributed to the Italian resident on a look-through basis and regardless of the existence of mid-layer non-CFC companies. Income of the CFC is therefore proportionally attributed to the Italian controlling shareholder and redetermined according to the provisions of the ITA. This means that dividends received by the CFC from a non-CFC third company benefit in the hands of the Italian resident controlling shareholder of the same treatment provided for white-list

dividends. [155]

In contrast, the same cannot be said in case of application of Art. 168 ITA concerning qualified but non-controlling participations in blacklist companies. In this case, income of the CFC is determined as the higher of:

- income resulting from the P&L account; and
- income resulting from the application of standard rates of return to the book value of the assets of the CFC.

As clarified by the Tax Agency in Ruling No. 326/E of 30 July 2008, such a mechanism overcomes the provisions of the ITA and dividends received by the CFC and inserted in its P&L account have to be taxed in their entirety.

Dividends actually distributed by the CFC corresponding to profits that were already attributed to the Italian resident shareholder are not taxable. The amount of dividends distributed exceeding those of the imputed profits, on the contrary, is subject to full taxation. [156]

With the goal of sparing double taxation, the cost basis in the shares of the CFC is increased for the amount of profits taxed on a look-through basis and decreased by the amount of dividends actually distributed by the CFC up to the amount of attributed profits. Foreign taxes paid by the CFC upon the profits attributed to the Italian shareholder on a look-through basis benefit of the foreign tax credit.

Profits produced by a blacklist permanent establishment of a white-list subsidiary undergo CFC taxation, [157] but it will be possible for the resident shareholder to prove that such profits actually underwent adequate taxation in the white-list country where the subsidiary resides. [158]

17.5.3. Domestic anti-abuse rules with respect to dividends sourced in tax havens

Dividends from unqualified stock in blacklist companies undergo full taxation in the tax return and, for ensuring the actual enforcement, in case of individual recipients also suffer an advance withholding tax of 12.5%. [159] If the blacklist company is listed, however, dividends from unqualified stock enjoy the 12.5% substitutive regime in case of individual recipients outside their business activity. After the 2006 reform, the same rule now also covers silent partnerships (in this case regardless of the enterprise being listed or not). [160]

Dividends from qualified blacklist stock received by individual entrepreneurs and partnerships are subject to an advance withholding tax upon their full amount, but if a waiver was obtained under Arts. 87(1)(c) and 167(5)(b) ITA, the advance withholding tax is applied only upon 49.72% of the amount, which is the taxable amount of the dividend (to be declared in the tax return): this is justified by the fact that Art. 87(1)(c) applies in case the Italian resident shareholder of the CFC proves that the income of the CFC was subject to an adequate level of taxation from the beginning of the holding period. All the above-mentioned withholding taxes are applied on the amounts received net of any foreign withholding tax paid at source. [161]

One may wonder whether applying the full taxation of the dividends from qualified stock of a blacklist company actually conforms to EU law, given that the partial exclusion from taxation is only granted in respect of profits distributed by companies that were subject to an adequate level of taxation on their income and not in respect of dividends coming from companies that were, although (tax-wise), duly operating abroad, under Art. 167(5)(a) ITA [162] do not suffer an "adequate" level of corporate taxation.

The practical incidence of such a question (after the exclusion of Malta and Cyprus from the Italian blacklist), however, can be tested only in relation to non-EU countries (no EU country is currently inserted in such a list) and under the freedom of movement of capital rather than the freedom of establishment.

Dividends originating from a blacklist company suffer full taxation, as the rationale for the partial exclusion consists in the avoidance of economic double taxation and the Italian legislator has seen no merit in integrating the shareholders' tax on the dividends with the negligible tax usually levied upon blacklist companies.

In this respect, after some changes of mind, the legislator reverted to the provision according to which dividends and similar income *originating* from blacklist companies undergo full taxation. [163] This counters the provision that was introduced by Legislative Decree 18 November 2005, No. 247 and suddenly repealed by Law Decree 4 July 2006, No. 223, according to which only dividends directly flowing into the hands of the resident holders of the securities from a blacklist company had to be taxed in full. As such a provision was manifestly prone to abuses and did not take into account that many white-list countries also did not tax those dividends when received by intermediate holding companies, the government rapidly came back to the old provision under which, regardless of the interposition of an intermediate holding entity, those dividends will be taxed in full in the hands of the resident holder when they are received. Such a rule only suffers two exceptions: the first, in relation to those dividends that relate to profits already

taxed in the hands of the resident shareholder under Italian CFC legislation; the second, in relation to dividends originating in a company for which a waiver of the CFC rules under Arts. 167(5)(b) and 87(1)(c) ITA was obtained.

17.5.4. Issues relating to the application of domestic withholding tax on outbound dividends

The application of the withholding tax on outbound payments of dividends and similar items of income is governed by Art. 27(3) of Presidential decree 600/1973. The withholding tax only applies insofar as the shares, securities or agreements from which the distribution derives are not effectively connected to an Italian PE of the non-resident recipient. [164] The withholding tax also does not apply to parent companies covered by the 435/90/EEC directive and shareholders companies covered by Art. 27(3ter) ITA. [165] The withholding rate is set at 27% and can be reduced under applicable tax conventions. The amount of the withholding rate is not affected by the level of shareholdings held by the recipient, nor by its nature: it is therefore irrelevant whether the non-resident shareholder is a company, an individual or another entity. As briefly mentioned at the beginning of this section, the levy is applied also on items of income which are considered like dividends for tax purposes, and thus to distributions made in favour of the holders of securities that are treated like shares under Art. 44(2)(a) ITA and in favour of a silent partner in case its contribution in the silent partnership does not consist in works and services.

Unlike in the case of the remuneration paid to security holders (whose debtor will always be a company or another commercial entity under Art. 73(1)(a) and (b) ITA), in the case of silent partnerships the withholding agent might also be an individual or a partnership. [166]

The withholding tax is also applied upon dividends relating to shares and securities deposited with an intermediary under the regime of asset management provided by Art. 7 of Legislative decree No. 461/1997.

The withholding rate is reduced to 12.5% in case of saving shares.

The withholding tax on outbound payments is also applied upon distributions of reserves other than reserves of profits: based on Art. 47 ITA, distributions made in favour of non-residents without an Italian PE follow the rules provided by the individual income tax: [167] according to these rules, in case of individual shareholders every distribution exceeding the cost basis is treated as a dividend distribution for tax purposes in the hands of the recipient. [168] In case of payments in kind, Art. 27(2) applies and therefore the recipient must provide the withholding agent with a cash amount equal to the tax to be paid over to the tax authorities. The amount of the withholding tax must be calculated upon the fair market value of the in-kind payment as assessed by the debtor at the time provided by Art. 109(2)(a) ITA. [169]

Foreign residents have a right to recover an amount of the withholding tax suffered at source in Italy equal to the amount of tax paid in their country upon the dividends or similar items of income, with the limit of one fourth of the withholding tax. [170] The reimbursement is denied in case the foreign residents are pension funds or taxpayers benefiting of the reduced withholding rates of 11% and 1.375%, as well as in case of savings shares (whose outbound dividends are subject to a withholding rate of 12.5%). Reimbursement requests by non-residents must be addressed to the *Centro operativo di Pescara*, which is the only office of the tax administration competent in this matter. [171]

Dividends and similar items of income not relating to an Italian PE are treated on a separate basis and do not enter into the business income of the foreign recipient, even when it has a PE in Italy. Italy does not provide for a force of attraction rule. [172]

Even when dividends (as well as other items of income such as interest) are received in connection with a business activity conducted by the non-resident recipient abroad they are treated on a separate basis and the source rules provide for their taxation any time they are distributed by an Italian resident company. [173]

Source rules on the taxation of capital gains on the shares of an Italian company are different; instead, as – apart from the application of the relevant provision of a bilateral convention (Art. 13(5) OECD Model) – they provide for the taxation in Italy, unless the capital gains relate to non-qualified stock [174] held in a listed company. In addition, no taxation occurs if the capital gains are realized by white-list non-residents upon non-qualified companies (regardless of the company being listed or not) and Art. 5(5) of Legislative decree 461/1997. [175]

Pursuant to Art. 27ter of Presidential Decree No. 600 of 29 September 1973, dividends paid on shares and similar instruments registered in the centralized deposit system (*Monte Titoli S.p.a.*) are not subject to the ordinary withholding tax under Art. 27 of the same Decree, but are instead subject to a final substitute tax, at the same rate and conditions as the withholding tax. [176] The provision is inspired by those contained in Legislative decree No. 239/1996 regarding bonds issued by so-called *grandi emittenti*. [177] The substitute tax is applied by banks, investment companies and all other intermediaries that are also in

charge of applying the substitute tax under Legislative decree 239/1996 participating in the Monte Titoli centralized deposit system. The substitute tax can also be applied by non-resident intermediaries directly or indirectly participating in the system through a duly appointed Italian fiscal representative.

Art. 1.68 of Law No. 244/2007 states that the application of the withholding rate of 1.375% (imposed by ECJ case law, see *supra*) can be applied only to dividends formed after 31 December 2007: as this is not in line with the above-recalled EU case law, the foreign shareholders undergoing higher taxation through the application of the substitute tax might file a request of refund for the taxes suffered in excess. Except in case of distributions of dividends subject to the final withholding tax of 12.5% in favour of resident taxpayers, the intermediaries participating in the system are also compelled to declare to the Italian tax authorities the data of the recipient, so that controls are permitted. [178] In order for the intermediary to be allowed to directly apply the reduced treaty rates, it is necessary to provide it with (i) a statement of the beneficiary of the dividends regarding the applicability of the convention and (ii) a certificate of residence issued by the tax authorities of the residence country (such certificate will be valid through 31 March of the following year). In case the reduced rate is applied, the shareholder is not entitled to the refund of one fourth of the tax provided under Art. 27(3) of Presidential decree No. 600/1973. The tax is not applied toward entities and international organizations that are tax exempt under specific international agreements or domestic law. The substitute tax is also not applied in case of applicability of the Parent-Subsidiary Directive, provided adequate documentation is collected proving that (i) all conditions are satisfied and (ii) a certificate of the foreign tax authorities is also collected stating that the form, residence and taxation regime of the parent company entitle it to the non-application of the withholding tax. The foregoing documentation must be kept by the intermediary for the entire period in which the Italian tax authorities are entitled to issue an assessment with respect to the tax year in which the dividends are paid or, if an assessment is issued, until the assessment is settled.

17.6. Selected issues of dividend taxation under EU law

17.6.1. Open issues in the implementation of the Parent-Subsidiary Directive

The Parent-Subsidiary Directive has been implemented in Italy through both Art. 27*bis* of Presidential Decree 600/1973 and Art. 89 ITA.

Art. 27*bis* of the Decree deals with the exemption from the Italian withholding tax on outbound dividends paid to EU-resident parent companies. Art. 89 ITA deals with the taxation of inbound dividends, inclusive of those paid by an EU-resident subsidiary qualifying for the application of the Parent-Subsidiary Directive.

With respect to inbound dividends, Art. 89 ITA does not recall the conditions for the application of the 95% dividend exclusion posed by the Directive, inclusive of that provided by Art. 2(1)(c); this might support the interpretation according to which dividends distributed by foreign companies are always subject to tax only upon 5% of their amount, regardless of the tax treatment of the distributing company. We shall recall in this respect that the ITA considers foreign entities as always opaque, so that, with the exception of CFCs, transparent taxation never applies, even when the foreign tax system treats the company as transparent for its own purposes. On the other hand, Art. 89 ITA refers to Art. 44(2)(a) ITA, under which shares and similar securities issued by foreign entities can be treated like domestic securities (and therefore their fruits be treated like dividends) when their remuneration is not deductible in the determination of the taxable income of the foreign distributing entity, thereby implicitly assuming that such an entity actually be subject to tax. And, indeed, the rationale of the partial exclusion would also support this second interpretation.

With respect to outbound dividend payments, Art. 27*bis* ITA exempts from the application of the withholding tax ordinarily applied with a rate of 27% all payments of dividends and any other item of income which is treated as a dividend under the ITA when the conditions set by Para. 1 are met, namely:

- (1) the foreign company has a direct participation in the share capital of the Italian distributing company of at least 10%; [179]
- (2) the foreign company is incorporated in the form of a company provided by the annex of the Parent-Subsidiary Directive;
- (3) the foreign company is fiscally resident in another EU country, also based on the applicable conventions against double taxation;
- (4) the foreign company is subject to tax in its country of residence and does not benefit of tax exemptions which are not limited territorially or in time; and
- (5) the foreign company has held the shares for a continuing period of 12 months before the receipt of the dividend.

With respect to the subject-to-tax requirement, it is important to stress that possible exemptions in favour of the foreign parent company do not affect the exemption from Italian withholding tax as long as they are limited, either territorially or in time. [180]

A mere reduction of the applicable tax rate on the income of the parent company should not affect the

application of the withholding tax. [181]

With respect to the application of the parent-subsidiary regime in favour of Swiss parent companies under Art. 15 of the EU–Switzerland Agreement of 26 October 2004, the Italian Tax Agency has denied the application of the exemption from withholding tax on outbound dividends in case the foreign parent is not subject to full taxation in Switzerland because it benefits of the exemption from the payment of the municipal and cantonal income taxes, as such an exemption has also been condemned by the EU Commission in its decision of 13 February 2007 as a State aid in contrast with the good functioning of the Agreement between the EEC and Switzerland signed on 22 July 1972. [182]

An important limit to the application of the exemption on outbound dividends originally derived from the requirement described under point 1) above: as the parent company needed to have a direct participation in the share capital of the distributing entity it may be understood that dividends were the only income which may benefit of the exemption, while payments of income of a similar nature (e.g. from a silent partnership or from securities that are otherwise treated as shares, also for tax purposes) did not. [183] Such a limitation has been repealed after the implementation of Directive 123/2003/EC through the introduction of Art. 27*bis*(1*bis*), which now extends the exemption to the distributions that are considered as similar to dividends tax-wise (i.e. income from silent partnerships and from securities that are treated like shares for tax purposes). Preferred shares and non-voting shares may benefit of the exemption. In case of repo transactions, the exemption may be applied only in favour of the cash seller. [184]

Participations held indirectly do not count for the achievement of the minimum threshold, while those held through a fiduciary company do. [185]

As in other countries, it has been debated whether the exemption only applies to dividends distributed during the ordinary activity of the company or also to liquidation proceeds. [186] The majority of the EU Member States has correctly implemented the Parent-Subsidiary Directive by granting the exemption from withholding tax also to the liquidation proceeds at the level of the subsidiary. The inclusion of liquidation proceeds within the scope of Art. 5, with the consequence of the exemption from withholding tax in the country of the subsidiary, clearly results from both the literal and the systematic interpretation of the Directive on the basis of the following reasons.

In the first place, Directive 2003/123/CE of 22 December 2003, which modified the Parent-Subsidiary Directive 90/435/CEE, states in its preliminary remarks at point 1): "Directive 90/435/EEC(3) introduced common rules in relation to dividend payments and other profit distributions, which are intended to be neutral from the point of view of competition." Such sentence cannot be interpreted other than admitting that the directive also applies to profits distributions different from "ordinary" dividends distributions and which also include liquidations distributions. The following point no. 2) is even more direct and unequivocally states that: "The objective of Directive 90/435/EEC is to exempt dividends and other profit distributions paid by subsidiary companies to their parent companies from withholding taxes."

In this respect, even Art. 4(6) of the circular of the Italian Ministry of Finance No. 26 of 16 June 2004, relating to the benefit of exemption from withholding tax under Art. 27*bis* of Presidential decree No. 600/1973, speaks about "distributed profits" and includes in such a definition interest which is recharacterized as dividends according to the rules on thin capitalization (Art. 98 ITC).

Furthermore, Art. 4 of Directive 90/435/CEE, as modified by Directive 2003/123/CE, provides: "Where a parent company or its permanent establishment, by virtue of the association of the parent company with its subsidiary, receives distributed profits, the State of the parent company and the State of its permanent establishment shall, except when the subsidiary is liquidated ... refrain from taxing such profits...." Such provision thus implies that the notion of distributed profits normally also includes those profits arising from liquidation. Art. 5 of Directive 90/435/CEE, as also modified by Directive 2003/123/CE, provides: "Profits which a subsidiary distributes to its parent company shall be exempt from withholding tax."

Therefore, on the basis of literal interpretation we must reach the conclusion that profits arising from liquidation fall within the scope of Art. 5 of the Directive and thus must be exempted from withholding tax at source. We must also reach the same result based on the systematic interpretation of the Directive, taking into account the ratio of its promulgation by the EU.

Indeed, the system construed by Arts. 4 and 5 of the Directive is justified by the goal of the EU legislator to avoid multiple taxation of the same kind of profits distributed upon the liquidation from an EU subsidiary to its EU parent company (once through the corporate income tax paid by the subsidiary, once through the withholding tax on profits paid by the subsidiary upon the liquidation and once, finally, through the corporate income tax paid by the parent company on the receipt of such profits) and, under an approximation of the CIN, assign the power to tax business income at the country of source (i.e. where the subsidiary is located). In this respect, it is irrelevant that some Member States have excluded from taxation the profits received by the parent company from its subsidiary under all circumstances, thereby allowing an even more favourable treatment than Art. 4 of the Directive provides to such profits. Indeed,

the Directive establishes an option, not an obligation, for the Member State of the parent company to tax such liquidation profits.

The goal of the Directive is to avoid double taxation of distributed profits. With respect to liquidation profits, it attributes the taxing power exclusively to the state of the parent company. Should we adopt a different interpretation, we would come to the absurdity that the Directive itself triggers multiple taxation of the same profits.

It must be stressed that Art. 4(6) of the above-mentioned Circular No. 26/2004 of the Italian Ministry of Finance, concerning the exemption from withholding tax foreseen by Art. 27*bis* of Presidential decree No. 600/1973, states that the benefit is to be given to *utili da partecipazione* (profits from the participation in companies).

The notion of *utili da partecipazione* in the Italian tax system refers to both "ordinary" dividends and "liquidation dividends and dividends from redemption of shares (Arts. 44 and 47 ITC). Thus, Art. 27*bis* should be correctly interpreted in the sense of including liquidation proceeds within the scope of the exemption from withholding tax.

It should also be noted that at the international level, Art. 10 of the OECD Model with its Commentary (Para. 28) expressly states that liquidation proceeds are to be considered such as dividends for international and withholding tax purposes.

That said, we shall also mention that the Italian Tax Agency took a different view on the occasion of an unpublished ruling.

From the point of view of anti-avoidance, the last paragraph of Art. 27*bis* states that the exemption applies in favour of a parent company that in turn is directly or indirectly controlled by a non-EU resident company, provided the EU parent company proves that it was not constituted with the only or main aim of taking advantage of the exemption. As clarified by the government report to the provision, the goal is to impede the transfer of the dividends free of tax toward an EU country which has a more favourable bilateral convention for the repatriation of the profits in the non-EU country of the ultimate parent company. The letter of the provision is not clear on the extent and nature of the control that the non-EU ultimate parent company must exert on the EU parent company claiming the benefits of the directive. Some authors also envisaged the possibility that the denial of the exemption could be extended to those EU parent companies whose majority of the share capital is held by non-EU shareholders, even if they are not connected to each other. [187]

The provision thus introduces an inversion of the burden of the proof, so that it is on the taxpayer to prove that the parent company actually conducts an active business in the country where it is located, even in the form of active management of the assets it holds in its quality of holding company. [188]

With reference to procedural issues we shall recall that the application of the exemption from withholding tax on outbound dividends may be achieved either directly or by way of reimbursement.

In order to be entitled to directly apply the directive, all conditions set by Art. 27*bis* above must be fulfilled at the time the payment is made, inclusive of the one concerning the minimum holding period of 12 months. [189] In addition, the withholding agent must collect from its parent company the following documentation:

- a certificate of fiscal residence of the parent company with the specification that the parent company is constituted in one of the forms provided by the Annex to the directive and is subject to taxation as provided by the directive, without benefiting of exemption regimes that are not limited in time or territorially; and
- the proof that the minimum holding period of 12 months has been completed.

The direct application of the exemption is made under the responsibility of the withholding agent, so that in case of reassessment by the tax authorities it will be responsible for the omission to apply and pay the tax to the tax authorities. [190]

Dividends paid before the completion of the 12-month minimum holding period are subject to the withholding tax but the parent company (as well as the subsidiary) [191] may file a request for reimbursement as soon as the period is completed. [192] The request has to be filed within 48 months after the application of the levy. [193] The documentation to be filed together with the request is the same as mentioned above for the direct application of the exemption.

Directive 435/90/EEC does not contain a provision requiring the taxpayer to obtain any kind of certification, neither prior to the payment of dividends nor afterwards. It would thus be perfectly in line with the directive that a system puts the burden to collect the data and information necessary to check the correct application of the directive on the tax administration, also through the exchange of information (regulated by Directive 77/799/EEC as modified per Directive 2003/48/EC). Italy, however, introduced as

a specific and *additional* requirement compared to those imposed by the Parent-Subsidiary Directive that before the payment of the dividends, the withholding agent obtains certain documents and a certification confirming the fulfilment of the substantial requirement for the application of the exemption. Such additional requirement could be brought before the authorities of the EU for having them declare it not in line with EU law, as it clearly limits the exercise of EU freedoms (in particular the freedom of establishment under Art. 49 of the Treaty of the EU). The only provision allowing Member States to integrate the provisions of the directive, indeed, is Art. 1(2) of the Directive, according to which, "2. This Directive shall not preclude the application of domestic or agreement-based provisions required for the prevention of fraud or abuse." That said, it is well known that all provisions of the Member States that affect principles and provisions of EU law must be *proportionate*. It is indeed beyond any doubt that disallowing the application of the Parent-Subsidiary Directive only based on the absence of a formal certificate that was nonetheless promptly provided upon request of the investigating tax authorities would be contrary to the spirit of EU law and by far disproportionate compared to the goal pursued by the same domestic provision imposing the release of such certificate prior to the payment (Art. 27bis(2) and (3), Leg. Decree No. 600/1973). The impression is also that when Art. 1.2 of the directive allows Member States to introduce provisions against fraud and abuse it does not in any manner refer to the necessity of providing formal certifications that the substantial conditions for the exemption from withholding tax are met. Art. 1(2) of the Directive, in fact, specifically refers to provisions that are meant to counter *material* violations of the spirit of the directive, and it should also be mentioned that Italy implemented this provision through Art. 27bis last paragraph (concerning the application of the exemption with respect to companies that are further controlled by other companies that, however, are not EU-resident; the provision has the clear objective of countering elusive triangulations and treaty shopping). Also, the decision of the ECJ in the *Denkavit* case of 17 October 1996 (Joined Cases C-283/94, C-291/94 and C-292/94) indirectly supports these conclusions, as in that case the Court stated that even though the "substantial" conditions (such as the minimum holding period) for the non-application of the withholding tax were not fulfilled at the time the payment was made, nonetheless the parent company was to be allowed to file a request of reimbursement once such conditions were completed (i.e. when the minimum holding period was completed), also with respect to payments of dividends that occurred before such period was completed. In fact, also under Italian tax law, violations which do not trigger tax evasion because they are only formal in character cannot be punished (Art. 10(3) of Law 212/2000, so-called "Bill of taxpayer's rights"). More specifically, Art. 6(5bis), Legislative decree 472/1997, states that violations that do not hamper the capacity of the authorities to control and do not affect the determination of the taxable base, of the taxes due or the payment of the tax cannot be punished. With specific respect to the possibility to apply the exemption from withholding tax also in the absence of the required documentation, the literature has sustained that the absence of the documentation, while the substantial conditions are met, should not impede to directly benefit of the exemption, as the release of the documentation is meant to provide the withholding agent with an excuse against any reassessment by the tax authorities (*Assonime*, Circular letter No. 63 of 1994, p. 33). According to the literature, the release of the documentation is intended to justify the non-application of the withholding tax by the withholding agent; once the subsidiary has obtained the documentation mentioned by Art. 27bis it will escape any sanction or reassessment by the tax authorities, as the absence of the substantial conditions for applying the withholding tax (thus, in contradiction with the documentation collected) could not be detected by the subsidiary. This does not mean that the withholding agent, under its responsibility, cannot decide to apply the exemption even before having obtained the documentation (directly applying the exemption is indeed always done under the direct responsibility of the withholding agent, which is also jointly liable for the payment of the tax under Art. 35, Pres. Decree 602/1973; see also, inter alia, Ministry of Finance, Circular letter No. 288/E of 6 November 1997).

For inbound dividends, Art. 89 refers to the notion of dividends contained in the ITA. Arbitrages on inbound dividends and similar income are limited by the requirement that the payment not be deductible for the foreign distributing entity. On the other hand, for outbound payments, there may be cases where a payment which is deductible for Italian tax purposes is treated as a dividend in the country of residence of the recipient entity. This could possibly occur, for instance, concerning a profit participating loan without the character of a silent partnership for Italian tax purposes. [194]

17.6.2. Issues of compatibility of domestic law with the EU law

As mentioned above, with respect to corporate taxpayers receiving dividends the ITA does not discriminate between domestic and inbound dividends, nor between dividends distributed from an EU subsidiary and those distributed by a non-EU subsidiary. The level of participation in the share capital of the company is also irrelevant, so that no discrimination of any kind may be seen in the regime of taxation of dividends received. [195]

The same could not be said concerning outbound dividends and similar payments. Up until the start of an infraction proceeding against Italy on 22 January 2007 and the consequent modification of Art. 27 of Presidential decree 600/1973, dividends distributed and similar payments to EU-resident corporate

shareholders not qualifying for the application of the Parent-Subsidiary Directive were indeed subject to the full withholding tax of 27%. Such a treatment was considered to be discriminatory, [196] considering that Italian corporate shareholders would be taxed on 5% of the dividends received in any case, regardless of the fulfilment of the requirements posed for the non-application of the withholding tax on outbound payments. The infraction proceedings resulted in a declaration by the ECJ of discrimination [197] and of the violation of the freedom of movement of capital. [198] Meanwhile, as mentioned above, the Italian government had modified the discriminatory provision, so that, as of 1 January 2008, [199] distributions made in favour of EU and EESA companies resident in a country granting an effective exchange of information for tax purposes are subject to a withholding tax of 1.375%, which is equal to the actual tax burden suffered by resident companies on the same item of income. [200] The withholding tax obviously refers only to dividends and similar income (inclusive of silent partnerships and securities that are treated like shares for tax purposes) paid to these companies not in connection with a PE of theirs in Italy (in which case taxation would be applied on the PE). [201]

An analogous discrimination was perpetrated to the detriment of foreign resident pension funds, as Italian pension funds were actually subject to a substitutive levy of 11% on their income, inclusive of dividends and similar items of income, while foreign pension funds were subject to the ordinary withholding rate of 27%. Art. 24(1) of Law 88 of 2009 eliminated such discrimination (already detected by the Commission; see press release No. IP/07/1152 of 23 July 2007); the current withholding rate on foreign pension funds resident in an EU country or in an EESA country granting exchange of information is set at 11%, the same rate of tax levied on Italian resident pension funds. [202]

Based on the decision of the ECJ on 18 June 2009 (Case C-303/07, *Aberdeen*), the Italian regime imposing a withholding tax of 27% on outbound payments of dividends and similar income received by non-resident investment funds may be considered in violation of EU law, and in particular of the freedom of establishment and of the freedom of movement of capital under Arts. 49 and 63 TFEU, since Italian resident funds and funds that are treated similarly for tax purposes are exempt from income taxation (the quota holder being taxed upon distributions or sales at a gain of its quotas).

With respect to the previous imputation system adopted by Italy up until 2003, on 9 January 2003, the EU Commission announced a formal request to the Italian authorities to terminate the levy of a withholding tax on dividends paid to parent companies resident in the Netherlands (Case C-2005/4047); [203] indeed, the Italian regime would be contrary to the exemption from withholding tax provided for by the Parent-Subsidiary Directive (90/435/EEC).

In fact, the proceeding originated from a decision of the Italian Supreme Court regarding the tax period 1998. In that year, the Italian regime for the taxation of dividends was based on the tax credit system, coupled with an equalization tax aimed at impeding that the shareholders received dividends paid out of tax-exempt profits and at the same time benefit from the tax credit (which was meant to eliminate double taxation and thus should not automatically apply in cases where no taxation occurred at the company level). In its decision No. 19152 of 26 April 2004, the Supreme Court affirmed that the tax treaty between Italy and the Netherlands allowed the levy of a withholding tax on outbound dividend payments such as that in that case (dividends paid from an Italian subsidiary to its Dutch parent company). The withholding tax was said to be applicable even though the payment would have otherwise qualified for the Parent-Subsidiary Directive regime.

In fact, the Supreme Court stated that Art. 7(2) of the Directive allows such withholding taxes because it states that Art. 5(1) of "the Directive shall not affect the application of domestic or agreement-based provisions designed to eliminate or lessen economic double taxation of dividends, in particular provisions relating to the payment of tax credits to the recipients of dividends." The statement was based on the decision of the ECJ in the case of *Océ van der Grinten* (Case C-58/01). The decision led to the opening of the infraction procedure as the Commission considered the interpretation of Art. 7(2) of the Parent-Subsidiary Directive adopted by the Italian authorities and by the Supreme Court as too extensive. In particular, the *Océ van der Grinten* case actually concerned the case of a distribution from the United Kingdom to the Netherlands, which suffered a tax treatment not comparable to the Italian treatment of an analogous distribution. In the Italian case, the reimbursement concerned the equalization tax, which was actually not meant as a means to lessen or eliminate double taxation, but rather as a means to restore ordinary taxation after the distributing company had taken advantage of some exemption from taxation of its profits. As the distribution of dividends did not trigger any dividend tax credit, the equalization tax should not apply, and thus be reimbursed. This did not justify the application of a withholding tax on the dividends as allowed by the convention, as the distribution of dividends was not coupled with a dividend tax credit (but rather only with the reimbursement of the equalization tax): hence, there was actually no overlap between conventional and Community methods (i.e. Art. 5 of the Directive) for eliminating double taxation: there was therefore no room for applying Art. 7(2) of the Directive as well.

Recently, this time in line with the principles of *Océ van der Grinten*, the Supreme Court has stated, with respect to Art. 10(4)(b) of the convention between Italy and France of 1989, [204] that a French company

cannot, at the same time, claim the application of the Parent-Subsidiary Directive and of the double tax convention. [205] Thus, even if at the time of the distribution the French parent company enjoys exemption from the Italian withholding tax based on the Directive, when it later files a request of refund of the tax credit provided under Art. 10(4)(b) of the treaty it has to undergo the application of the domestic withholding tax (reduced to 5% as per Art. 10(2) of the treaty) upon the whole distribution (therefore of both the original dividend received [206] and of the dividend tax credit provided under Art. 10(4)(b) of the treaty).

17.7. Selected issues of dividend taxation under tax treaties

According to Art. 10(3) of the OECD Model Convention, "dividends" means "income from shares, 'jouissance' shares or 'jouissance' rights, mining shares, founders' shares or other rights, not being debt-claims, participating in profits, as well as income from other corporate rights which is subjected to the same taxation treatment as income from shares by the laws of the State of which the company making the distribution is a resident."

As specified in Paras. 23 and 24 of the Commentary to Art. 10, such list of examples is not exhaustive, given the great differences between the laws of the OECD member countries. Although the OECD definition does not necessarily match with Italian law, the scheme provided by Art. 10(3) is generally adopted in Italian conventions, according to which a general definition of the concept of dividends comes with a non-exhaustive list of examples, together with – in an enlarged view – other types of incomes that have, in the state of residence, the same tax treatment as income from shares.

It may be useful in this sense to compare the explanations contained in the Commentary to the OECD Model with the definitions of Art. 44 ITA [207] in order to highlight the converging points and the possible departures. For this purpose, it should be borne in mind that, pursuant to Art. 169 ITA, the national law remains applicable if more favourable to the taxpayer, as well as when derogating to the provisions of an international convention.

First, Art. 10 of the OECD Model comprehends shares, jouissance shares or jouissance rights, which are certainly included within the domestic definition of Art. 44(1)(e) ITA, which considers capital shares and property shares.

There is, on the other hand, a contrast between domestic law and the OECD Model as regards founders' shares. Art. 53 ITA treats the participations in profits of the founders as self-employment income. [208] While the literature considers applicable in such cases the advantages provided by the convention for the distribution of dividends, [209] it should be recalled that non-resident founders may claim the lack of territoriality as per the domestic rules. [210]

In the phrase "other rights, not being debt-claims, participating in profits", there may be included the profits deriving from the participating financial instruments as covered by Arts 2346(6), 2349(2) and 2447ter(1)(e) CC. [211]

Besides, Art. 2351 CC regulates special types of shares, namely:

- non-voting shares;
- shares with limited voting rights;
- shares whose voting rights are conditioned upon the occurrence of future events; and
- shares whose voting rights are grouped in echelons according to the number of shares held (*azioni con voto a scalare*).

Moreover, the following can be issued:

- shares non-proportional to capital contributions (*azioni non proporzionali*); [212]
- preferred shares (*azioni privilegiate*); [213]
- deferred shares (*azioni postergate*); [214]
- tracking shares, which have financial rights corresponding to the results of the company's activities in a particular field (*azioni correlate*); [215]
- redeemable shares (*azioni riscattabili*); [216] and
- shares of a limited liability company with particular administrative rights (*quote di società a responsabilità limitata con particolari diritti amministrativi*). [217]

Such types of financial instruments are included within the extended conventional definition of "shares" or of "other rights, not being debt-claims, participating in profits", or of the closing clause that assimilates to dividends "the income from other corporate rights which is subjected to the same taxation treatment as income from shares by the laws of the State of which the company making the distribution is a resident", because they are precisely "corporate rights" and thus subjected in Italy to the same treatment of the shares.

Para. 24 of the Commentary to Art. 10 of the OECD Model excludes the application of Art. 10 to interest

payments on convertible bonds and on participating loans. However, Para. 19 of the Commentary on Art. 11 states that "the interest on such bonds should be considered as a dividend if the loan effectively shares the risks run by the debtor company". [218]

As regards Italian law, Art. 2411(1) CC states that the bondholders' rights to repayment of capital and interest may be subordinated to the rights of other creditors. The timing and the extent of the payment of interest may vary, pursuant to Art. 2411(2), in accordance with objective criteria, based on the performance of the company. Despite the definition as "bonds" (*obbligazioni*) used in the Code, the characteristics of such financial instruments make them more similar to atypical securities (*titoli atipici*), although they seem to be subjected to the tax regime that is applicable, pursuant to Art. 44(1)(c) ITA, to "bonds". Should the interpretation that considers them as bonds also for tax purposes prevail, the non-resident taxpayer will most likely prefer the domestic characterization to that provided by the convention, given that the tax regime of interest paid to the non-resident bondholders is generally more favourable than that applied to dividends. [219] On the other hand, should the atypical securities interpretation prevail, the non-resident will most likely claim for the application of the dividends regime of the double tax convention. [220]

Art. 2411(3) CC refers to financial instruments that are similar to bonds, where the time and the extent of the payment of capital are based on the financial performance of the company. Such securities should benefit from the reduced withholding tax rate established by the conventions for the taxation of dividends in the state of source, given the definition of "dividend" in Para. 25 of the Commentary to Art. 10, which does not prevent the treatment of this type of interest as dividends under the domestic rules on thin capitalisation applied in the borrower's country. [221]

The definition provided in Art. 10(3) of the OECD Model is significant, especially with reference to the profits paid to a subject who is resident in the other contracting state because, should Art. 10 be applicable, the beneficiary could obtain a partial reimbursement of the withholding tax up to one fourth of the latter as per Art. 27(3) of Presidential decree No. 600/1973, provided the "dividends" have been taxed in the foreign residence country. [222] The definition may also be relevant for foreign-source dividends received by a resident when the convention establishes particular benefits for the resident beneficiary; this is the case of the treaties signed with Brazil and Germany, which totally exempt from taxation in Italy those dividends deriving from such states if they are paid to a corporation or to another Italian commercial entity that holds at least 25% of the capital of the foreign company. [223]

The case is different regarding bonds regulated under Art. 2411(2) CC, which states that the time and the extent of the payment of interest may vary in accordance with objective criteria, as well as based on the economic performance of the company. Such income should be considered as interest for treaty purposes, given the definition in Art. 10(3) of the OECD Model, under which debt claims fall outside the scope of application of the provision. [224] The same applies under Art. 6 of Directive 2003/48/EC. [225]

On the contrary, it is believed that the wording of Art. 10(3) could not be claimed in order to characterize as dividends foreign items of income that are not considered as such under domestic law. [226] This could result in a different characterization of the same item of foreign-source income for treaty purposes and for the purposes of domestic taxation in the hands of the recipient. The case may be, for example, that a distribution of dividends by a foreign company be treated as a distribution of dividends for foreign withholding tax purposes and as a distribution of income from an investment fund, or a payment of interest, for Italian tax purposes.

The case may also be, for example, that a vehicle that is treated as a company under the laws of the state of source cannot be treated as such under the laws of the state of residence of the shareholder. The fact that for treaty purposes such vehicle will be considered as a company under Art. 3 of the OECD Model and that Art. 10 of the Model will therefore apply, does not compel the same treatment to be granted with respect to the taxation of the distributions in the hands of the shareholder/quota holder who is resident in the other contracting state. This is a likely outcome in the case of investment funds, which are sometimes organized under a corporate or a partnership structure; in other cases, investment funds can be organized as trusts or they may even take the form of a contract. [227] This was also made clear by CONSOB, according to which a Swiss company that filed a request for listing on the Italian Stock Exchange:

[S]eems comparable to a collective investment fund.... And in fact, such company simply and only conducts an activity of investment in hedge funds taking advantage of an organization which is under all aspects comparable to the one characterizing collective investment funds (investment manager, investment advisor, investment custodian), and also uses a depository bank. The ultimate goal of such an activity is to increase the amount of the funds that have been collected on the open market through the continuous investment/divestment of the financial instrument contained in its portfolio, and thus the collective management of the funds aimed at maximizing the return on the investment of the investors. In other words, leaving aside the formal characterization of the company as such under Swiss law, where the vehicle was incorporated, in the case at hand all elements that characterize the Community law definition of

an investment fund are manifest. [228]

Also, under Italian law, [229] an investment fund is “the autonomous assets collected, thorough one or more issuances, among a plurality of investors with the goal of investing such assets on the basis of a pre-set investment policy, divided into quotas pertaining to a plurality of participants, collectively managed, in the interest of the quota holders and autonomously from the same participants.” Therefore, the Italian definition of investment fund also disregards the form and looks to the functions actually performed by the vehicle. This leads to the need to analyse the characterization of a given vehicle on a case-by-case basis, [230] as is also done in other jurisdictions. [231] Even though with reference to Italian investment funds, the Tax Agency has recently clarified that a vehicle lacking one of the characteristics described by the above-mentioned regulatory provisions will not be treated as a fund for tax purposes either. [232] The Tax Agency has remarked that in order to be qualified as a fund, an investment vehicle has to be participated by a plurality of investors, although indirect stakes may also be considered (e.g. when the fund only has one investor, which, however, represents a plurality of investors, as in the case of a pension fund). [233]

In general terms, the distinction between the participation in a company and in an investment fund should be based on a variety of criteria, such as: (i) quota holders of a fund actually have a credit toward the fund for the value of their investment and their participation in the fund can be distinguished from the participation in a company; shareholders, in fact, enjoy greater rights than investors, in particular concerning the management of the company; [234] (ii) the remuneration of a shareholder is based on the actual profits realized by the company and accounting rules are very strict on the possibility to make distributions in the absence of adequate and final realized profits; the remuneration of the investors in a fund is linked more to the current net asset value of the fund, which is subject to fluctuations and valuations in a greater degree than the profits of a company; (iii) the right of exit, e.g. by way of redemption, is usually stronger for an investor in a fund compared to a shareholder; (iv) investment funds need a depositary bank for their assets and such a bank is often in charge of some control and monitoring on the compliance with investment policy by the managers of the fund; and (v) from a purely fiscal perspective, income from a fund is treated as income from capital under Art. 44(1)(g) ITA, thus not under the same heading of dividends (Art. 44(1)(e) ITA).

As far as interest payments are concerned, the Tax Agency has never given any formal instructions on whether Art. 10 or 11 of the OECD Model should apply in case of the application of the now-repealed rules on thin capitalization. According to the Commentary (Para. 25 to Art. 10), the existence of such rules should not impede the application of the treaty article on dividends: those payments are to be treated as dividends for the purposes of application of the laws of the source state. [235]

Art. 10 of the OECD Model should also apply to income derived from a silent partnership, as such income falls within the definition of “other rights, not being debt-claims, participating in profits”.

As regards the anti-abuse rules, the wording of the provisions of some of the double tax conventions signed by Italy reflects the OECD Model, while others differ from it. [236] In this context, among the anti-avoidance provisions, there are both general and specific treaty anti-abuse measures. As regards the former category, some of the Italian literature [237] supports the existence of an unwritten rule against treaty shopping, which is considered as the practice of some investors in unduly seeking the application of a more favourable tax treaty through the use of conduits and shell companies that do not present sufficient substantial connections with the state where they are incorporated, especially in connection with the receipt of flows of passive income. [238] Such behaviour being in contrast with the general spirit of bilateral conventions, taxpayers resorting to such schemes are prevented from taking advantage of the treaty. This can be done in various ways. At the level of the treaty itself, limitation on benefits (LOB) clauses aim at denying treaty benefits in absence of sufficient links with the country of incorporation. An example of an LOB clause is the one included in the 1984 treaty concluded with the United States, which was then also inserted in the new convention. [239]

Another example of an LOB clause is given by Art. 29 of the treaty signed between Italy and San Marino (21 March 2002, but not yet in force) which states that, “notwithstanding the other provisions of the present Convention, a person that is resident of a contracting State shall not be entitled to relief from taxation in that other contracting State if it was the main purpose or one of the main purposes of the creation or assignment of such resident to take advantage of the provisions of this Convention.” [240] While LOB clauses have been under scrutiny for possible breach of the freedom of establishment and of the principle of non-discrimination under EU law, [241] the ECJ has considered the LOB clause contained in the Netherlands–United Kingdom treaty as compatible with EU law. [242]

Rather than through detailed LOB clauses, Italy has tried to counter tax avoidance and treaty shopping by inserting the OECD beneficial ownership clause in most of its post-1977 treaties and by applying domestic anti-avoidance principles and provisions. [243]

The meaning of “beneficial owner” under Arts. 10, 11 and 12 of the OECD Model remains one of the major concerns for both the OECD organization [244] and the domestic system.

Since the introduction of the clause in the 1977 version of the Model Convention, the commentary made clear that “the limitation of tax in the State of source is not available when an intermediary, such as an agent or nominee, is interposed between the beneficiary and the payer.” An amendment was made in 1995 in order to clarify that the benefits of the treaty should nonetheless be granted if, in spite of the interposition of an agent or nominee, the beneficial owner was also a resident of the other contracting state. The OECD Committee on Fiscal Affairs had already underlined in its 1987 Report on “International Tax Avoidance and Evasion” [245] that the limitation of tax in the state of source cannot also be applied to those other cases where a person enters into contracts or takes over obligations under which it has a similar function to those of a nominee or an agent, thereby expanding the scope of application of the anti-avoidance clause beyond the limits of agents and nominees. According to the clarifications inserted in the 2003 Commentary to the OECD Model, the beneficial ownership clause was introduced to clarify the meaning of the words “paid ... to a resident” as they are used in Art. 10(1), in the light of the scope of the double taxation conventions. In fact, “[t]he term ‘beneficial owner’ is not used in a narrow technical sense, rather, it should be understood in its context and in light of the object and purposes of the Convention, including avoiding double taxation and the prevention of fiscal evasion and avoidance.” [246] Thus, a “conduit company” cannot be regarded as the beneficial owner if, though the formal owner of certain assets, it has very narrow powers which render it a mere fiduciary or an administrator acting on account of the interested parties.

As specified in the Report of the OECD Committee on Fiscal Affairs on “Double Taxation Conventions and the Use of Conduit Companies”, [247] there is no coincidence between a conduit company and the beneficial owner because the former “has, as a practical matter, very narrow powers which render it, in relation to the income concerned, a mere fiduciary or administrator acting on account of the interested parties”. Recently, in April 2011, the Committee has proposed some changes to Arts. 10, 11 and 12 of the OECD Model with reference to the beneficial owner definition, affirming that, when the beneficial ownership clause was introduced in Art. 10(1) to clarify the meaning of the words “paid ... to a resident” as they are used in that paragraph, “it was intended to be interpreted in this context and not to refer to any technical meaning that it could have under the domestic law of a specific country.” [248] Thus, “the domestic law meaning is applicable to the extent that it is consistent with the general guidance in this Commentary.” Moreover, according to the proposed changes, it would be specified that “the recipient of a dividend is the ‘beneficial owner’ of that dividend where he has the full right to use and enjoy the dividend unconstrained by a contractual or legal obligation to pass the payment received to another person.”

It must be noted also that if the beneficial owner is resident in a third state with which the state of source has concluded a convention, it will benefit from the provisions of such convention. [249]

With reference to the beneficial owner definition, the literature has identified different interpretations: [250]

- the definition provided by common law, simply transferred into the OECD Model;
- a meaning that excludes only agents and nominees, which are the examples expressly provided by the Commentary;
- thirdly, the “beneficial owner” could be considered as the person to whom income is attributed according to the domestic legislation of the contracting states; and
- lastly, beneficial ownership could be interpreted according to an autonomous definition to be specifically used for treaty purposes, in the light of the object and purposes of the convention.

It has been held that the term “beneficial owner” cannot be interpreted with reference to the domestic law of the state which applies the bilateral treaty under Art. 3(2) of the OECD Model, given that no legal system provides for a clear definition of the terms “beneficial owner”, “*bénéficiaire effectif*” or “*Nutzungsberechtigter*”.

The literature [251] now agrees in considering such terms with an autonomous meaning for treaty purposes, that has to be interpreted based on the “object” and “purposes” of the Convention. In particular, Vogel considers that treaty benefits should not be granted to a person who is only formally entitled to the receipt of dividends, but rather a substance-over-form approach should prevail.

Apart from those provisions which have implemented EU rules (this is the case, for instance, of the directives on interest from savings and on interest and royalties payments between associated companies), the Italian legal system does not provide for a statutory definition of “beneficial ownership”. Such concept, however, is underlying other provisions, such as Art. 37(3) of Presidential Decree No. 600 of 1973 (see below) and the same Art. 1 ITA.

Also, case law [252] still does not provide for a clear-cut definition and interpretation of the concept, which seems to be used in narrow or broader sense depending on the specific facts of the case. Although one should take into account such an outcome when it comes to general concepts of anti-avoidance – judges are there for concretely applying general concepts to the specific fact patterns of a given case – such a lack of guidance may result in questionable decisions and legal uncertainty. [253]

Italian literature generally embraces the perspective of the most authoritative international literature previously mentioned, [254] giving to the beneficial ownership concept an autonomous definition to be specifically used for treaty purposes, in the light of the object and purposes of the convention, i.e. avoiding double taxation and preventing fiscal evasion and avoidance.

According to other opinion, the beneficial ownership concept has to be interpreted under an economic meaning, as is the case of the Interest and Royalties Directive (2003/49/CE). [255] In this context, the Tax Agency, although expressly referring to interest and royalties under Arts. 11 and 12 of the OECD Model, consider the “beneficial owner” concept with reference to the economic entitlement (substance-over-form approach). [256]

Lastly, others believe that the concept of beneficial owner has to be referred to the person to whom the income is attributable for tax purposes (*fiscalmente imputabile*), i.e. an intermediary, acting as an agent or nominee, between the actual beneficiary and the debtor cannot be regarded as the beneficial owner. In order to benefit of the treaty, being fiscally “resident” in the other contracting state is sufficient, once the recipient is “liable to tax”, while it is not required that the recipient is also actually “subject to tax”. [257] This is the opinion held in the OECD Partnership Report and in Resolution No. 104/E of 1997 of the Italian Ministry of Finance. [258]

It is worth noting that some treaties, such as those with Japan (20 March 1969) and India (19 February 1993) do not provide at all for such a clause. Art. 10(5) of the Italy–United Kingdom treaty (21 October 1988), on the other hand, states that the provisions relating to the refund of the dividend tax credit [259] shall not apply “unless the recipient of a dividend shows ... that the shareholding in respect of which the dividend was paid was acquired by the recipient for bona fide commercial reasons or in the ordinary course of making or managing investments and it was not the main object nor one of the main objects of that acquisition to obtain entitlement to the tax credit....” This is an example of a specific anti-abuse rule, similar to the provision that can be found in the France–Italy treaty of 5 October 1989. [260]

The co-existence of general and specific anti-abuse rules can also be found in domestic law. In particular, the Italian tax system provides for a general anti-abuse rule under Art. 37*bis* of Presidential Decree of 29 September 1973, No. 600, whereas, in 2008, the Supreme Court [261] stated that a general abuse of law principle arises directly from Art. 53 (ability to pay) and Art. 3 (equality) of the Italian Constitution.

As confirmed by the literature, in particular after the changes to the Commentary in 2003, tax treaties do not prevent the application of domestic anti-abuse rules. [262]

As regards the general anti-abuse domestic rules, according to Art. 37*bis* of Presidential Decree No. 600/1973, the tax authorities may disallow the tax advantages unduly obtained through any act or transaction carried out without valid economic reasons and for the purposes of circumventing obligations or prohibitions contained in Italian tax law for obtaining a tax saving. Pursuant to Art. 37*bis*(3), this applies only if the tax advantage results from:

- mergers, divisions, transformations and liquidations and distributions to shareholders of reserves not consisting of profits;
- contributions to companies and transactions for the transfer or utilization of business assets;
- transfers of debt claims and tax credits;
- EU mergers, divisions, transfers of assets and exchanges of shares;
- transactions concerning securities and financial instruments; or
- transfers of assets between companies within the same consolidated tax group.

The scope of such provision has been expressly extended by the Italian legislator to payments of interests or royalties made to persons who are directly or indirectly controlled by one or more persons established outside the EU, [263] whereas the payment of dividends is governed by the specific anti-avoidance clause contained in Art. 27*bis*(5) of Presidential decree No. 600/1973, according to which the exemption from withholding tax at source provided by the EU Parent-Subsidiary Directive (435/90/EEC) cannot be granted if the sole or main purpose of the creation of the recipient mother company was to achieve such tax treatment.

Both Art. 37*bis* and the general principle of anti-avoidance envisaged by the Supreme Court’s decisions of 2008 can be applied and in fact are applied in connection with the illegitimate use of double tax conventions, for instance for countering conduit schemes and dividend washing and stripping schemes, sometimes overruling specific and more detailed provisions that could actually be applicable as well, [264] such as e.g. Art. 37(3) of Presidential decree No. 600/1973, which specifically deals with fictitious interpositions. The flavour of the most recent case law is that the general principle of anti-avoidance envisaged by the Supreme Court could be applied together (or regardless) of more specific anti-avoidance rules contained in tax treaties, inclusive of the beneficial ownership clause. [265]

Most of the treaties signed by Italy have a provision similar to the following:

The taxes collected in a State by means of withholding at source shall be refunded on request of the person interested or of the State of which he is a resident where the right to levy the taxes is limited by the provisions of this Convention.

Refund requests, to be filed within the terms established in the law of the State from which the refund is due, must be substantiated by an official statement made by the State of which the taxpayer is a resident saying that the conditions established in order to benefit from the exemption or the reductions provided for in the Convention have been met.

The competent authorities of the Contracting States shall establish, by mutual agreement, in accordance with the provisions of Article 26 of this Convention, the particulars for the application of this Article. [266]

Moreover, such treaties generally leave room for the domestic provisions, sometimes by specifying that claims for reduction or refund shall be made within the limits set by the law of the contracting state which has to grant the reduction or refund and that the competent authorities of the contracting states shall by mutual agreement settle different modes of the application of the procedural issues. Indeed, the OECD Commentary also suggests that the procedural issues should be left to the discretion of the member countries. [267]

Direct application of the reduced rates or exemptions provided by the convention is always admitted (by way of a general and unilateral concession of the Italian authorities), but the withholding agent remains jointly liable for possible mistakes and the subsequent recovery of the taxes due. [268]

As regards the documentation that has to be submitted as an adequate proof of the conditions required, the instructions given by the Italian tax authority to the withholding agents' tax return (Form 770) state that the withholding agent who did not apply the (full) withholding tax, "has to keep and exhibit or submit, if required by the Tax Agency, the certificate released by the competent foreign tax authority which proves the residence of the recipient, and the documentation proving the existence of the conditions required for the application of the conventional regime." In some cases, the competent authorities of the other contracting state have agreed with Italy for particular forms, which in substance require documents equivalent to those required by the above-mentioned instructions. [269] It is still debated whether the taxpayer also has to prove that the flows of income are not connected to an Italian PE; while the original position of the Italian authorities was to require such a proof, [270] the above-mentioned instructions to Form 770 do not include such a requirement.

According to Ruling No. 126/E of 26 July 1999, the certificate issued by the foreign authorities only has to certify the status of the recipient as a liable to tax resident of the other state, while the other conditions for the application of the reduced withholding rates, like the fact the recipient is the beneficial owner or that the dividends are not connected with an Italian PE, can be self-declared by the taxpayer, who will be held responsible in case of false statement. [271] Some conventions also provide for instructions in case the request of refund is filed by someone who is not the beneficial owner of the payment (e.g. a fiduciary company). [272] The formal transfer of the shares to a fiduciary company, does not preclude the direct application of the convention, nor of the Parent-Subsidiary Directive. [273]

In those cases where a further reduction of the treaty rate is conditioned upon minimum thresholds of shareholdings or minimum holding periods, the proof to be substantiated by the taxpayer may be given in various ways, including a statement by the depositary bank that the shares have been continuously held without interruptions, or via an excerpt of the shareholders' registry of the company. [274] The documentation should normally be acquired by the withholding agent before the payment is made, [275] even though there would be no grounds for denying treaty benefits based only on a delay in the collection or delivery of the documentation to the tax inspectors, also considering that, as noted above, the withholding agent will be held liable for possible violations.

Requests of refund must be filed, either by the withholding agent or by the taxpayer, within 48 months from the application of the withholding tax [276] with the *Centro Operativo di Pescara* of the Italian Tax Agency. [277]

Based on the different wording of the conventions with France [278] and with the United Kingdom, [279] Italian case law has drawn a difference regarding the deadline for filing a request of reimbursement. While in the case of French taxpayers, the request of refund could be filed within the ordinary statute of limitations of 10 years (Art. 2946 CC), in the case of UK shareholders, such request should be filed within the 48-month time limit provided by tax law (Art. 38, Presidential decree 602/1973). [280]

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1. Partner, Studio Uckmar Associazione Professionale, Milan and Genoa; Harvard Law School International Tax Program; admitted to the New York Bar; PhD in private law, University of Pisa.

2. Simonetto, E., "Società, contratto a prestazioni corrispettive e dividendo come frutto civile", *Banca borsa e titoli di credito* 1 (1962) p. 487; Boero, P., *Articolo 669*, in Delfini F. and Cuffaro V. (eds.), *Commentario al codice civile*, Milan, 2010, p. 775.
3. The reform was introduced by Legislative Decree No. 6 of 17 January 2003 (published in the *Gazzetta Ufficiale* No. 17 of 22 January 2003, "*Riforma organica della disciplina delle società di capitali e società cooperative, in attuazione della legge 3 ottobre 2001, n. 366*", modified by Legislative Decree No. 37 of 6 February 2004, effective from 1 January 2004, and then also by Law No. 262 of 28 December 2005).
4. Art. 2364, according to which, in a company without a supervisory board, the regular meeting, among other things, approves the financial statements. However, pursuant to Art. 2433, if the financial statement is approved by the supervisory board according to Art. 2364bis, the decision on the distribution of profits is also for the latter. See Campobasso, G.F., *Diritto Commerciale*, vol. 2, Torino, 2009; Presti, G. And Rescigno, M., *Corso di diritto commerciale*, Vol. 2, Bologna, 2009; Colombo, G.E. and Portale G.B., *Trattato delle società per azioni*, Vol. 7, Torino, 1994.
5. In the case of S.p.A.s based on the two-tier system, the balance sheet is drawn up by the management board and then submitted for the approval of the supervisory board. However, the resolution on distributing profits is not adopted by the supervisory board but by a shareholders' meeting. In this sense, see *Corte di Cassazione*, 28 May 2004, No. 10271, *Giust. civ. Mass.*, 2004, 5; *Tribunale di Trani*, 19 September 2000, *Società*, 2001, 481.
6. Galgano, F., *Trattato di diritto commerciale e di diritto pubblico dell'economia*, Padova, Vol. VII, 2006.
7. Art. 2430 CC.
8. *Organismo Italiano di Contabilità (OIC)*, Accounting Principle No. 20 - *Titoli e partecipazioni* (September 2005): generally, on an accrual basis, the relevant moment is when the shareholders are entitled to receive dividends as a result from the decision adopted by the members' meeting. Cf. Accounting Principle No. 21 - *Il metodo del patrimonio netto* (November 2005).
9. Art. 2553 CC.
10. The contract of *cointeressenza impropria* thus overlaps with the definition of silent partnership, the only difference being that under the latter, absent a different agreement between the parties, the silent partner does not participate in the losses of the enterprise. See Piazza, M., *Guida alla fiscalità internazionale*, Milano: Il Sole 24 Ore, 2004, p. 428, also for additional reference.
11. Art. 2411.1 CC.
12. Among the more recent contributions, see Notari, M., "Partecipazione al rischio di impresa, strumenti finanziari e categorie giuridiche", *Strumenti finanziari e fiscalità* 1 (2011) p. 13.
13. McCormick, R. and Creamer, H., *Hybrid Corporate Securities: International Legal Aspects*, London, 1987, p. 2.
14. A recent and interesting case was represented by the Italian so-called "Tremonti bonds" (similar programmes for the management of the financial crisis were adopted abroad as well). See below for a description of their characteristics and their tax treatment.
15. Notari, M., op. cit., p. 15.
16. Art. 5 ITA.
17. Tax Agency, Circular letter 16 June 2004, No. 26/E, Para. 2.
18. Art. 2346(6) CC provides that a company may issue financial instruments conferring economic or also administrative rights in return for contributions made by a shareholder or by a third party, which may also consist of works or services.
19. Note the absence of any definition of the term "group", which gives rise to uncertain interpretation; e.g. it is not clear at what point in time the existence of a group should be considered, in particular between the issue date and the date of receipt of income; also, it is not clear what definition of group should be used, as different provisions of the ITA refer to different definitions of the term "group" (e.g. for consolidation purposes and for transfer pricing purposes or for CFC purposes etc.).
20. Art. 109(9)(a) ITA.
21. Art. 109(9)(b) ITA.

22. Legislative Decree 1 September 1993, No. 385.
23. Tax Agency, Circular letter 16 June 2004, No. 26/E, Para. 2.3.
24. Note that while these securities are defined as bonds in the heading of the provision, the same provision thereafter always refer to them as "securities". See also the implementing decree of the Ministry of Finance, 25 February 2009.
25. In this respect, among others, see Corasaniti, G., Giannelli, A. and Strampelli, G., "I cosiddetti 'Tremonti Bond': profili societari, fiscali e contabili", *Strumenti finanziari e fiscalità* 1 (2011) p. 129.
26. CONSOB (*Commissione Nazionale per le Società e la Borsa*) is the public authority responsible for regulating the Italian securities market; ISVAP (*Istituto per la Vigilanza sulle Assicurazioni Private e di Interesse Collectivo*) is the regulatory authority competent for the insurance sector.
27. *Documento Banca d'Italia-Consob-Isvap*, 21 July 2009, No. 3, *Tavolo di coordinamento fra Banca d'Italia, Consob ed Isvap in materia di applicazione degli IAS/IFRS*.
28. See Corasaniti, G., in Corasaniti-Giannelli-Strampelli, op. cit.: such position was also based on the accounting treatment of the securities for IAS purposes, which, before the introduction of Art. 5 of the Ministerial decree 8 June 2011, prevailed, according to the majority of the authors, over the Income Tax Act based on Art. 83 ITA (contra: see Escalar, G., "Azioni, quote di partecipazione e strumenti finanziari simili", in Zizzo, G. (ed.), *La fiscalità dei soggetti IAS/IFRS*, Milano, 2011; that said, according to this author, even without taking into account the IAS accounting of these securities, their remuneration might be seen as strictly linked to the economic performance of the issuing banks under Art. 44(2)(a) ITA. Stevanato, D., "Il regime fiscale dei Tremonti bond", *Corriere tributario* (2009) 1026, on the contrary, supports the characterization as debt instruments, as he does not see a sufficient link of the remuneration to economic performance of the bank under Art. 44(2)(a) ITA. Stevanato also anticipated in this respect the content of Art. 5 of Ministerial decree 8 June 2011, which finally clarified the prevalence of the ITA provisions on the characterization of the debt and equity instruments over those relevant for IAS purposes according to Art. 83 ITA. That said, as mentioned above, it is debatable whether, notwithstanding the prevalence of the ITA requirements over those of the IAS, the Tremonti bond should cease being treated as equity for tax purposes after the introduction of Art. 5 of Ministerial decree of 8 June 2011.
29. No payment will be made if the bank does not make a sufficient profit.
30. As noted above, the remuneration will be paid within the amount of distributable profits. See in this respect, Tax Agency, Circular letter 16 June 2004, No. 26/E, Para. 2.3. It should also be recalled that unlike interest payments, the remuneration of Tremonti bonds is not cumulative, and therefore those amounts "accruing" in a given year are foregone, in the absence of all conditions set for the payment to be allowed.
31. Circular letter No. 4/E of 18 January 2006.
32. See Art. 23 of the Germany-US treaty, signed on 29 August 1989, as amended through the Exchange of Notes signed on 17 August 2006 (in particular, by Art. XII(4) of the protocol). See, in particular, the Technical Explanation, according to which, "The so-called 'switchover clause' is intended to deal with cases of double exemption of income (e.g., through the granting of a dividends paid deduction to the U.S. payor of a dividend and a correlative exemption of such dividend in Germany)."
33. Art. 44(2)(a) ITA.
34. This under Art. 6(2) ITA, according to which payments made in substitution of an item of income enjoy the same tax treatment of the latter income.
35. Besides the ITA, it is important to recall that important rules on the taxation of dividends "and the like" are contained in Presidential Decree 29 September 1973, No. 600.
36. Art. 47(1) ITA and Ministerial Decree 2 April 2008.
37. Art. 3(3)(a) ITA and Art. 27, Presidential Decree 600/1973.
38. Art. 2(6) of Law decree No. 138 of 13 August 2011, converted into Law No. 148 of 14 September 2011. In relation to the application of the withholding tax of 11% on dividends distributed to EU- and EEA-based pension funds as per Art. 27(3) of Presidential decree 600/1973 (which might be repealed by the newly enacted provision, see Gusmeroli, M., "Quer pasticciaccio brutto della ritenuta sugli utili corrisposti a fondi pensione europei", *Boll. Trib.*, 18/2011, p. 1363, who underscores the mistake the Italian legislator incurred when it did not make an exception to the

- new 20% rate in relation to dividends paid to EU- and EEA-based pensions funds, while at the same time maintained a preferential 11% taxation on dividends received by Italian pension funds, which might revive the infraction proceedings that were opened prior to the enactment of Art. 27 (3), which made the taxation of foreign pension funds via withholding tax at source equal to the taxation of resident pension funds.
39. See Tax Agency, Circular letter 26/E of 2004, quoted above.
 40. Tax Agency, Circular letter 10 December 2004, No. 52/E, Para. 2.2.2.1.
 41. Art. 67(1)(c)(1) ITA.
 42. Art. 47(6) ITA.
 43. Art. 45 ITA.
 44. See the Government Report under Art. 4 of Legislative Decree 461/1997.
 45. Italian Ministry of Finance, Circular letter No. 74/E of 1994. Such kind of constructive taxation of the dividends lays upon the theory of the so-called *incasso giuridico*.
 46. *Commissione tributaria centrale*, 3 October 1990, in *fisconline* and *Cassazione*, 6 September 2004, No. 17925, *Giust. civ. Mass.*, 2004, p. 9.
 47. *Cassazione*, 29 April 2009, No. 10030, on *fisconline*.
 48. Note that some authors support the view that even in case such a qualification of the missing collection of the dividends had to be done, the amounts to be taxed should be taxed as a dividend, not as interest, under the rule that provides that income paid in substitution of other income follows the same rules (Art. 6(2) ITA): see Corasaniti, G., "Commento all'Art. 27 del d.p.r. 600/1973", *Commentario breve alle leggi tributarie*, Padova, Vol. IV, 2011.
 49. Tax Agency, Circular letter 26/E of 2004, Para. 3.1, op. cit.
 50. Art. 18 ITA and Art. 23 of the relevant conventions against double taxation signed by Italy.
 51. See the Communication of 19 December 2003, COM(2003) 810 final, Para. 3.2.4. See also below for further discussion of this issue.
 52. ECJ, 14 November 2006, Case C-513/04, *Kerckhaert and Morres*; 16 July 2009, Case C-128/08, *Damseaux*. See Tarigo, P., "Principio generale comunitario di eliminazione della doppia imposizione, libertà fondamentali e obblighi convenzionali: il caso *Damseaux*", *Rassegna Tributaria* 5 (2010) 1477; Valente, P., "Trattamento dei dividendi nella sentenza Jacques Damseaux", in the database *Fisconline*.
 53. Art. 27(4bis) of Presidential Decree 600/1973.
 54. Art. 165.10, ITA. Please note that under Art. 27.4.a of the Presidential Decree 600/1973 in case of qualified foreign stock held by an individual outside her business activity an advance withholding tax of 12,5 per cent will apply on the taxable amount of the dividend; the taxpayer will then enjoy a credit for such an amount in her tax return.
 55. Although they do not always fall under the rules for the taxation of business income, non-commercial entities do benefit of the partial exclusion from the taxation on dividends under Art. 4.1.q, Legislative decree 344 of 2003, regardless of the nature of their activities.
 56. Art. 27, Presidential decree 600/1973.
 57. The Parent-Subsidiary Directive 434/90/EEC was implemented in the Italian legislation through Art. 27bis of the Presidential decree 600/1973. Italy has adopted the exemption method and not the credit method. The taxation of 5% of the dividends received is seen as a forfeit compensation for the deduction of the costs connected to the management of the participation. The exemption from withholding tax on outbound dividends is denied if the shareholding company is fictitiously interposed by a non-EU controlling shareholder which could not take advantage of the directive (Art. 27bis.5, of the decree).
 58. ECJ, 19 November 2009, Case C-540/07, *Commission v. Italy*. The challenge of the Italian discrimination for the treatment of outbound dividends paid to entities subject to the corporate tax and resident in another EU country or in a EESA country was based on the previous case law of the ECJ: in particular, see 14 December 2006, Case C-170/05, *Denkavit*, in which the ECJ stated that regardless of the application of the Parent-Subsidiary Directive, Arts. 43 and 48 of the Treaty forbid the application of a heavier levy on outbound dividends compared to that applied on domestic distributions. See also, with respect to the freedom of capital flows, the judgment of 8 November 2007, Case C-379/05, *Amurta*.

59. See below for a further analysis.
60. See Circular letter No. 32/E of 8 July 2011.
61. See, among others, *Cassazione*, 4 December 2006, No. 25688 and 8 July 2008, No. 18640, in the database *fisconline*. The latter decision stated that the fact that the company incurred a loss has no bearing on the taxation of the constructive dividends, unless the shareholders prove that the hidden income received another (non-taxable) destination, such as reinvestment in the company. The former decision stated that the constructive dividend should be taxed in the same tax period the undeclared profits were realized by the company, as no formal approval by the shareholders' meeting will ever take place in such cases. On privately held companies, see Uckmar, V., *Le società a ristretta base azionaria*, Padova, 1955.
62. See the Commentary to Art. 9 of the OECD Model, Paras. 8 and 9.
63. In the Italian literature, see Valente, P., *Manuale del transfer pricing*, Milan, 2009, pp. 818-820.
64. The first provision that tried to counter the use of these schemes was Arts. 14(6bis) and 14(7bis) ITA (introduced by Law decree 9 September 1992, No. 372), which, under the previous credit method regime, denied the recognition of the credit for the underlying corporate tax in case the seller of the shares could not take advantage of such credit (e.g. because it was not subject to the income tax or because it was a non-resident). After the 2004 reform and the introduction of the exemption method, Art. 109(3bis) et seq., introduced through Art. 5quinquies of Law decree 30 September 2005, No. 203, converted into Law 2 December 2005, No. 248, now bar the deduction of losses realized on the sale of shares for an amount equal to the amount of dividends that enjoyed the 95% exclusion from taxation in the preceding 36 months.
65. Supreme Court, decisions 30055, 30056 and 30057 of 23 December 2008, in the database *fisconline*.
66. See the paragraph below dedicated to these taxpayers.
67. *Commissione Tributaria Regionale Lombardia*, 29 March 2011, No. 45.
68. This holds true also in the case of IAS adopters: see Italian Tax Agency, Circular letter 7/E of 28 February 2011, Para. 4.4.
69. Mignarri, E., "Le novità antielusive sulle *stock option* e sui contratti pronti contro termine", *Bancaria*, 6 (2007) p. 38 and on *Fisconline*; Dragonetti, A., Piacentini, V. and Sfondrini, A., *Manuale di fiscalità internazionale*, Milano, IVa ed., 2010, p. 638 et seq. Trabucchi, "La rilevanza fiscale del *manufactured dividend* - brevi riflessioni *de jure condito* e *de jure condendo*", *Dialoghi di diritto tributario* (2007) p. 1008.
70. Art. 83 ITA, as of 1 January 2008.
71. See the most recent instructions by the Tax Agency, released with Circular letter 28 February 2011, No. 7/E. In the literature see, inter alia, Zizzo, G., *La fiscalità delle società IAS/IFRS*, Milano, 2011. See also Ministerial decree 8 June 2011 and Ministerial decree 1 April 2009, No. 48.
72. Art. 85(3bis) ITA.
73. Art. 89(2bis) ITA.
74. Art. 94(4) ITA.
75. Escalar, G., "Il regime fiscale di azioni, quote e strumenti simili per le società *IAS adopter*", in Zizzo, G. (ed.), *La fiscalità delle società IAS/IFRS*, Milano, 2011, Chap. 6. Corasaniti, G., "Il coordinamento tra disposizioni fiscali e principi contabili internazionali e gli strumenti finanziari", *Corriere tributario* 27 (2011) 2198.
76. Under IAS 32: "An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities.... When an issuer applies the definitions in paragraph 11 to determine whether a financial instrument is an equity instrument rather than a financial liability, the instrument is an equity instrument if, and only if, both conditions (a) and (b) below are met.
 - (a) The instrument includes no contractual obligation:
 - (i) to deliver cash or another financial asset to another entity; or
 - (ii) to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the issuer.
 - (b) If the instrument will or may be settled in the issuer's own equity instruments, it is:
 - (i) a non-derivative that includes no contractual obligation for the issuer to deliver a variable

- number of its own equity instruments; or
- (ii) a derivative that will be settled only by the issuer exchanging a fixed amount of cash or another financial asset for a fixed number of its own equity instruments. For this purpose, rights, options or warrants to acquire a fixed number of the entity's own equity instruments for a fixed amount of any currency are equity instruments if the entity offers the rights, options or warrants pro rata to all of its existing owners of the same class of its instruments do not include instruments that have all the features and meet the conditions described in paragraphs 16A and 16B or paragraphs 16C and 16D, or instruments that are contracts for the future receipt or delivery of the issuer's own equity instruments.

A contractual obligation, including one arising from a derivative financial instrument, that will or may result in the future receipt or delivery of the issuer's own equity instruments, but does not meet conditions (a) and (b) above, is not an equity instrument. As an exception, an instrument that meets the definition of a financial liability is classified as an equity instrument if it has all the features and meets the conditions in paragraphs 16A and 16B or paragraphs 16C and 16D.... A financial instrument that does not explicitly establish a contractual obligation to deliver cash or another financial asset may establish an obligation indirectly through its terms and conditions. For example:

- (a) a financial instrument may contain a non-financial obligation that must be settled if, and only if, the entity fails to make distributions or to redeem the instrument. If the entity can avoid a transfer of cash or another financial asset only by settling the non-financial obligation, the financial instrument is a financial liability.
- (b) a financial instrument is a financial liability if it provides that on settlement the entity will deliver either:
 - (i) cash or another financial asset; or
 - (ii) its own shares whose value is determined to exceed substantially the value of the cash or other financial asset.

Although the entity does not have an explicit contractual obligation to deliver cash or another financial asset, the value of the share settlement alternative is such that the entity will settle in cash. In any event, the holder has in substance been guaranteed receipt of an amount that is at least equal to the cash settlement option (see paragraph 21)."

- 77. Although the decree is silent on this, the literature considers that IAS-adopting taxpayers should also apply the rules provided for atypical securities, i.e. those securities that do not fall in the category of shares and similar securities nor in the one of bonds and similar securities. Atypical securities are regulated by Arts. 5 and 6 of Law Decree 30 September 1983, No. 512, converted into Law 25 November 1983, No. 649.
- 78. Arts. 117-129 ITA.
- 79. Arts. 130-142 ITA.
- 80. See Italian Tax Agency, Circular letter 20 December 2004, No. 53/E and the government report accompanying the reform.
- 81. In any case, a single company may not, at the same time, participate in more than one consolidation regime.
- 82. Art. 118(4) ITA. These payments include those for the transfer of interest expense in excess of the limits posed by Art. 96 ITA for their deduction by the single company that sustained it. These payment are also irrelevant for VAT purposes (Art. 3(3)(a) of Pres. Decree 633/1972) and registration tax purposes (Tax Agency, ruling 12 July 2007. No. 166/E), unless they exceed the value of the tax benefit (Circ. Letter 53/E of 2004, quoted above).
- 83. Art. 1(33)(t), Law 24 December 2007, No. 244.
- 84. The option is valid only if both the company and all of its shareholders make the election (Art. 4 of Ministerial decree 23 April 2004).
- 85. Art. 115(1) ITA. The shareholders, on the contrary, are not barred from also entering a consolidation regime, both as consolidating and as consolidated entities (Art. 1(3) of Ministerial decree 23 April 2004).
- 86. Art. 115(2) ITA and Art. 1(2), Ministerial decree 23 April 2004.
- 87. In particular, losses can be transferred to the shareholders only up to the proportional quota of the net equity of the transparent company (Art. 115(3) ITA).
- 88. The shareholders' meeting can validly choose to distribute prior reserves (Art. 115(5) ITA).
- 89. Art. 115(5) ITA.
- 90. Art. 115(12) ITA.

91. Art. 170(3) ITA.
92. Art. 5 ITA.
93. Art. 170(4) ITA.
94. Art. 170(5) ITA.
95. Art. 171(1) ITA.
96. Converted into Law 27 February 1998, No. 30.
97. Art. 160 ITA; see also Italian Tax Agency, Circular letters 19 February 2008, No. 12/E, Para. 11 and 21 December 2007, No. 72/E.
98. For a list of the connected activities which may enjoy the tonnage tax regime, see Ministerial decree 23 June 2005, in particular Art. 6.
99. Art. 157(2) ITA.
100. Art. 156 ITA and Art. 12 of Ministerial decree 23 June 2005.
101. Law 27 December 2006, No. 296.
102. Law 24 December 2007, No. 244. See also Ministerial decree 7 September 2007, No. 174 and the regulation issued by the Director of the Tax Agency on 28 November 2007. See also the official instructions released by the Italian Tax Agency with the Circular letter 31 January 2008, No. 8/E.
103. After the notification of the infraction proceeding No. 2008/4524, Italy has eliminated the violation of EU law under which the SIIQ regime was granted only to Italian resident companies. Art. 12 of Law decree 25 September 2009, No. 135, converted into Law 20 November 2009, No. 166, made clear that the SIIQ regime is also applicable to EU and EESA companies resident in a country granting an effective exchange of information with a permanent establishment in Italy. Income of the PE from the favoured real estate activities will be subject to a substitutive tax of 20%.
104. Such rate is further reduced to 15% in case of leasing of certain dwelling houses under Law 9 December 1998, No. 431; the goal is to favour access to convenient housing at affordable prices.
105. See Circular letter 8/E, quoted above, Para. 6.1.
106. Such an obligation is conditioned upon the SIIQ having sufficient profits to make a distribution under the general rules provided by the Civil Code; for example, no obligation to distribute will arise as long as the SIIQ has not set up sufficient legal reserves under Art. 2430 CC. In case the SIIQ produces both exempt and taxable income, such baskets will have to be used to set up the legal reserve on a proportional basis; see Italian Tax Agency, Circular letter 8/E of 2008, quoted above. Another example of forbidden distributions refers to losses that have affected the share capital: until its reconstitution no dividend can be paid (Art. 2433(3) CC) or to profits deriving from IAS valuations (Art. 6, Legislative Decree 28 February 2005, No. 38).
107. The requirement of such preponderance being 80%.
108. See Art. 2 of the directive; Circular letter 8/E, quoted above, Para. 6.1.
109. Italy only regulates closed-end real estate investment funds, whose fiscal regime has been recently reformed by Art. 32 of Law decree 78/2010. Among other changes, the new rules provide for the application of a withholding tax of 20% with respect to distributions in favour of non-residents other than white-list pension funds, white-list investment funds, states or international organizations and central banks and similar institutions. Instructions have been released by the Tax Agency with Circular letter 9 March 2011, No. 11/E. Residents of treaty partners have the right to undergo the reduced rate provided under Art. 11 of the double tax convention. Capital gains on the sale of the quotas undergo the ordinary rules, so that they are not taxable in Italy if they regard listed real estate investment funds or if the seller is resident in a white-list country.
110. Schenk, A. and Oldman, O., *Value Added Tax - A Comparative Approach*, Cambridge University Press, 2007. In particular, the authors recall the definition provided by the First VAT Directive 67/227/EEC: "The principle of common system of value added tax involves the application to goods and services of a general tax on consumption exactly proportional to the price of the goods and services, whatever the number of transactions which take place in the production and distribution process before the stage at which tax is charged. On each transaction, value added tax, calculated on the price of the goods or services at the rate applicable to such goods or services, shall be chargeable after deduction of the amount of value added tax borne directly by the various cost components".

111. See ECJ, 20 June 1991, Case C-60/90, *Polysar Investment Netherlands*, Para. 17; 22 June 1993, Case C-333/91, *Sofitam*, Para. 12; 10 June 1996, Case C-155/94, *Wellcome Trust Ltd v. Commissioners of Customs and Excise*. Although in relation to State aids, see also ECJ, 10 January 2006, *Cassa di risparmio di Firenze et al.*, Case C-222/04, concerning the special tax treatment of Italian foundations holding controlling stakes in Italian banks.
112. ECJ, 20 November 2000, Case C-142/99, *Floridienne and Berginvest*, Para. 19. See also *Cibo Participations* (Case C-16/00, 27 September 2001) and Terra, B. and Kajus, J., *A Guide to the European VAT Directives*, Amsterdam: IBFD Publications BV, 2011, Vol. 1.
113. ECJ, Case C-60/90, *Polysar Investment Netherlands*, op. cit., Para.
114. Del Federico, L., "Determinazione del pro rata nel caso di società holdings che effettuano operazioni esenti nei confronti di imprese consociate", *il fisco*, 19 (2001) p. 6986; Pistone, P., "Rassegna critica della giurisprudenza della Corte di giustizia in materia di imposta sul valore aggiunto (gennaio 2000-luglio 2001)", *Riv. dir. trib.*, 10 (2001) p. 137.
115. ECJ, Case C-60/90, op. cit.
116. ECJ, Case C-142/99, op. cit.
117. ECJ, Case C-16/00, op. cit.
118. ECJ, *Floridienne and Berginvest*, op. cit., Paras. 22-23.
119. ECJ, *Sofitam*, op. cit., Para. 13; *F. and B.*, Para. 21. The same result was reached with respect to interest received by a holding company on loans which it made to its subsidiaries, as according to the ECJ such interest should be excluded where the relevant loans did not constitute an economic activity of the holding company. See, among others, ECJ, 20 June 1996, Case C-155/94, *Wellcome Trust*, Para. 36.
120. ECJ, *Floridienne and Berginvest*, op. cit. According to Art. 17(5) of the Sixth Directive, which recalls Art. 19(1) of the same Directive (now Arts. 173 and 174 of the Directive 112/2006/EC - the Recast VAT Directive): "In the case of goods and services used by a taxable person both for transactions in respect of which VAT is deductible and for transactions in respect of which VAT is not deductible, only such proportion of the VAT as is attributable to the former transactions shall be deductible. Such proportion must be determined for all the transactions carried out by the taxable person. Article 19 provides that the deductible proportion must be made up of a fraction comprising (a) at the numerator, the total amount, exclusive of VAT, of the taxable transactions entered into as a seller or provider; (b) at the denominator, the total amount, exclusive of VAT, of transactions entered into as a seller or provider, inclusive those exempt from VAT."
121. ECJ, *Sofitam*, Para. 14.
122. An English version is available on the IBFD database (www.ibfd.org).
123. In fact, in order to meet the stage reached by the ECJ in its decisions mentioned so far, the Italian lawmakers introduced in 1997 relevant amendments through the Legislative Decree of 2 September, No. 313.
124. The Ministry of Finance has also clarified that in order to qualify as a taxable person, a holding company must possess, together with a non-commercial activity, which is not relevant for VAT purposes, an "adequate" structure dedicated to the taxable transactions (Circular Letter 24 December 1997, No. 328/E).
125. Del Federico, L., op. cit.; Ferrario, A., "Il diritto alla detrazione per le società 'holding'", *l'iva*, 1 (2002) p. 40; Stancati, "In tema di detrazioni iva da parte delle holdings" *Giurisprudenza italiana* 12 (2002) p. 2419; Fanelli, R., "Dividendi e interessi attivi non alterano il 'pro-rata' di una holding", *Corr. Trib.*, 5 (2001) p. 375; Salvini, L. "La detrazione iva nella sesta direttiva e nell'ordinamento interno: principi generali", in *Studi in onore di Victor Uckmar*, Padua, 1997, p. 1046.
126. See, inter alia, ECJ 13 March 2008, *Securenta*. Although in relation to exempt transactions, see, inter alia, ECJ, 6 April 1995, Case C-4/94, *BLP Group plc*, according to which: "[W]here a taxable person supplies services to another taxable person who uses them for an exempt transaction, the latter person is not entitled to deduct the input value added tax paid, even if the ultimate purpose of the exempt transaction is the carrying out of a taxable transaction. The wording of those provisions shows that to give rise to the right to deduct, the goods or services in question must have a direct and immediate link with the taxable transactions, and that the ultimate aim pursued by the taxable person is irrelevant in this respect." Once again, the case concerned the input VAT suffered by a holding company on advisory services connected with the sale of a 95% participation in a subsidiary (i.e. an exempt transaction when realized in the context of an

- "economic activity": see ECJ 29 April 2004, *EDM*). More recently, ECJ, 29 October 2009, Case C-29/08, *AB SKF*, according to which: "There is a right to deduct input value added tax paid on services supplied for the purposes of a disposal of shares, under Article 17(1) and (2) of Sixth Directive 77/338 ... if there is a direct and immediate link between the costs associated with the input services and the overall economic activities of the taxable person. It is for the referring court to take account of all the circumstances surrounding the transactions at issue in the main proceedings and to determine whether the costs incurred are likely to be incorporated in the price of the shares sold or whether they are among only the cost components of transactions within the scope of the taxable person's economic activities." See also the decisions 30 March 2006, Case C-184/07; 14 September 2006, Case C-72/05; 13 March 2008, Case C-437/06; 12 February 2009, Case C-515/07; 8 June 2000, Case C-98/98; 22 February 2001, Case C-408/98. In Italian case law, inter alia, *Cassazione*, 9 September 2008, No. 22690 and 9 June 2009, No. 13197.
127. See also Ministry of Finance, Circular letter 24 December 1997, No. 328/E, including as examples the advisory services paid in order to reorganize the corporate structure or to settle a litigation. See also, however, the decision of the ECJ in *BLP Group plc*, quoted above.
 128. ECJ, 26 May 2005, Case C-465/03. See also ECJ, 26 June 2003, Case C-442/01, *KapHag*.
 129. As noted by Terra and Kajus, op. cit., p. 1000, this is in line with the nature of VAT as a consumption tax. In line with such a nature of the tax, the ECJ adopted a strict interpretation of the concept of general overhead costs whose input VAT may be deducted in the *Investrand* case (Case C-435/05, 7 February 2007), where the VAT paid on advisory services was deemed to be connected to the safeguard of the assets (shares) of the holding company, rather than to its general (and VAT-taxable) activity: in absence of a direct and immediate link to the economic and VAT-taxable activity of *Investrand*, the ECJ therefore denied the deduction of input VAT.
 130. Terra and Kajus, cit., pp. 1013-1014.
 131. In this sense, see also Terra and Kajus, id., pp. 1015-1016. According to *Securenta*: "To the extent that input VAT relating to expenditure incurred by a taxpayer is connected with activities which, in view of their non-economic nature, do not fall within the scope of the Sixth Directive, it cannot give rise to a right to deduct. The answer to the first question must therefore be that, where a taxpayer simultaneously carries out economic activities, taxed or exempt, and non-economic activities outside the scope of the Sixth Directive, deduction of the VAT relating to expenditure connected with the issue of shares and atypical silent partnerships is allowed only to the extent that that expenditure is attributable to the taxpayer's economic activity within the meaning of Article 2(1) of that directive."
 132. Stancati, op. cit.
 133. See Ruling 13 May 1999, No. 77/E; Ruling No. 27/E of 2002, quoted above, and Circular letter 328/E of 1997, quoted above.
 134. De Ferra, "Dell'associazione in partecipazione", in Scialoja and Branca (eds.), *Commentario al codice civile*, Bologna, 1973, p. 6. Ricca, F., "Soggetti ad IVA gli utili percepiti dall'associato d'opera nell'associazione in partecipazione", *Corr. Trib.* 35 (2002) 3190; Comelli A., "Sul trattamento dell'associazione in partecipazione ai fini dell'Iva", *Giur. It.*, 7 (1997); Ficari V., "Presupposto oggettivo dell'IVA ed utili percepiti dall'associato nell'associazione in partecipazione fra imprenditori", in *Giur. It.*, 3 (1999).
 135. Among others, *Cassazione*, 18 June 1987, No. 5353; 25 February 1987, No. 2004; 5 October 1967, No. 2272; *Comm. Trib.* II degree of Bozen, 22 March 2007, No. 6; *Comm. Trib. Centr.*, 28 June 1995, No. 5997, which excludes the application of VAT also in case of participation of the contributor to the losses of the enterprise; 18 April 1996, No. 1806. Against the application of VAT, see *Cassazione*, 2 July 1998, No. 6466, based on the uncertainty of the return from the contribution in the silent partnership and the absence of proportionality between the value of the contribution and the return on the "investment".
 136. Italian Tax Agency, Resolution of 30 July 2002, No. 252/E - which recalls the previous Circular Letter of 28 October 1988, No. 221. In particular, the Tax Agency points out that the exclusion of the contribution paid to the silent partner from VAT was affirmed by the Supreme Court in its decision No. 6466/1998 with reference to facts prior to the amendments introduced by Legislative Decree No. 313/1997. See also, *Assonime*, Circular letter 17 April 2003, No. 21. For registration tax purposes, see Ministry of Finance, Circular letter 10 June 1986, No. 37/E, commenting on the 1986 registration tax reform, which provided that silent partnerships should be treated as exchanges rather than as corporate agreements.
 137. The Tax Agency also confirmed this interpretation also for past years, i.e. before the amendment of Art. 5 of the implementing decree through Circular letter 22 January 2008, No. 4/E; Fanelli,

"Irrilevanti anche per il passato per le prestazioni d'opera dell'associato in partecipazione", in *Corr. Trib.* 9 (1998) p. 743.

138. See Idsinga, F., Kalshoven, B.J. and Van Herksen, M., "Let's Tango! The Dance between VAT, Customs and Transfer Pricing", *International Transfer Pricing Journal* 5 (2005) p. 199, where the authors affirm that adjustments come in many flavours, yet there are two main routes, i.e. adjustments made (i) in the capital realm of the affiliated parties (by an additional dividend payment or capital contribution) or (ii) by retroactively increasing or decreasing the prices of the transactions between parties. In the former route, it can be said that for VAT purposes no transaction takes place, provided that, based on ECJ case law, dividends are not deemed to be consideration for a VAT taxable transaction (ECJ, Case C-77/01, 29 April 2004, *Empresa de Desenvolvimento Mineiro*). See also Lucas Mas, M.O., "Value Added Tax", in Bakker, A. and Obuoforibo, B. (eds.), *Transfer Pricing and Customs Valuation - Two worlds to tax as one*, Amsterdam: IBFD Publications BV, 2009.
139. Art. 2(2)(6) of Presidential decree No. 633/1972; see also Italian Tax Agency, Rulings No. 40/E of 13 May 2002; 194/E of 17 June 2002; 191/E of 23 July 2009; ECJ, 17 May 2001, Case C-322/99 and Case C-323/99.
140. Art. 4(1)(d)(1) of Part I of the Tariff attached to Presidential decree No. 131/1986, registration tax act; Ministry of Finance, Ruling No. 174/E of 2000.
141. Art. 4(1)(d)(1), Tariff, id.
142. Art. 4(1)(d)(2) and (1)(a)(4), Tariff, id..
143. Art. 4(1)(d)(2) and (1)(a)(3), of Tariff, id.
144. Galli, C., "Italy - Corporate Taxation", Sec. 14., in IBFD, *Country Analyses* (2011).
145. Id.
146. This goal of the system has been confirmed when the corporate tax rate was reduced to 27.5%. In order to retain the final amount of taxation in the integrated corporation/shareholder system, the amount of dividends excluded from taxation was reduced from 60% to 50.28%: see Ministerial decree 2 April 2008.
147. The rate will be increased to 20% as of 1 January 2012 as per Art. 2(6) of Law decree 13 August 2011, No. 138, converted into Law No. 148 of 14 September 2011.
148. See also Italian Tax Agency, Circular letter No. 26/E of 2004, Para. 4.3.
149. Although with respect to the particular case of income from savings, it is worth mentioning that the EU Directive on income from savings No. 48/2003, implemented in Italy by Legislative Decree No. 84/2005, has eliminated the double taxation on interest on savings. Art. 11 of the directive states that the Member State of residence is obliged to eliminate the double taxation on interest subject to the withholding tax applicable in Austria, Belgium and Luxembourg: the methods to be applied are the foreign tax credit or the refund procedure. Art. 10 of Legislative Decree No. 84/2005 provides that it is possible to recover the foreign withholding tax on interest, even if Art. 165 ITC is not applicable, because foreign interest is subject to the Italian withholding tax of 12.50% (20% as of 1 January 2012, see supra the quotation of Law decree 138/2011, Art. 2(6)). In that case, the Italian individual taxpayer may ask the Italian tax authorities for the refund of the entire withholding tax (15%, 20% or 35%) applied on interest in Austria, Belgium and Luxembourg, or to compensate it with other taxes to be paid by the Italian taxpayer: although it is expressly provided in Directive No. 48/2003 that the application of the Italian final withholding tax of 12.50% on interest may not be an obstacle to the elimination of the double taxation on interest subject to the withholding tax applicable in Austria, Belgium and Luxembourg.
150. ECJ, 14 November 2006, Case C-513/04, *Kerckhaert and Morres*; 16 July 2009, Case C-128/08, *Damseaux*, see supra note 52 for citation of the relevant Italian literature.
151. Communication of 19 December 2003, COM(2003) 810 final, Para. 3.2.4.
152. EU Commission, Consultation paper of 28 January 2011, "Taxation problems that arise when dividends are distributed across borders to portfolio and individual investors and possible solutions".
153. Art. 167 ITA. The control can be direct or indirect. After the reform introduced by Art. 13 of Law decree 1 July 2009, No. 78, converted into Law 3 August 2009, No. 102, Italy has mixed its previous jurisdictional approach to CFC legislation with a taint of the transactional approach. While income of companies resident in a blacklist country is always attributed pro quota to the Italian controlling shareholder, after the reform some items of passive income produced by white-

list companies may be subject to CFC legislation as well. One of the goals of the reform was to counter fictitious foreign residences or the fictitious attribution to foreign entities of assets producing passive income such as dividends, capital gains, interest, royalties and income from the provision of intra-group services. In line with ECJ, 12 September 2006, Case C-196/04, *Cadbury Schweppes*, some waivers may apply (Art. 167(5) ITA).

154. Art. 168 ITA.
155. See Italian Tax Agency, Ruling No. 51/E of 6 October 2010, which seems to overrule the preceding and opposite interpretation released in Ruling 18/E of 29 January 2003.
156. Arts. 47(4) and 89(3) ITA.
157. Art. 1(1), last sentence, of Decree No. 429/2001 implementing the CFC regime.
158. This conclusion derives from the wording of Art. 167(1) ITA, which refers to subsidiaries which are "resident or located" in a tax haven (emphasis added). The possibility to obtain a waiver is provided by Art. 167(5)(b) ITA and Art. 5(3), last sentence, of Decree No. 429/2001 implementing the CFC regime.
159. Unless a waiver under Arts. 87(1)(c) and 167(5)(b) ITA has been obtained proving that the income of the CFC has suffered an adequate level of taxation abroad from the beginning of the holding period.
160. Art. 27(4)(b) Presidential Decree 600/1973.
161. See Italian Tax Agency, Circular letter No. 4/E of 8 January 2006.
162. Such a provision excludes the application of the CFC rules in respect of companies that prove to actually conduct a business activity of an industrial or a commercial nature as their main corporate activity in the market of the foreign country or territory.
163. Art. 47(4) ITA.
164. Italian Tax Agency, Circular letter 16 June 2004, No. 26/E.
165. I.e. subject-to-tax companies resident in a EU country not covered by the Parent-Subsidiary Directive or in a EESA country which grants an effective exchange of information for tax purposes.
166. *Assonime*, Circular letter No. 32 of 2004, p. 71. Such an interpretation is also supported by Art. 14 (2) of Legislative decree No. 247/2005, which included individuals and partnerships among the withholding agents under Art. 27(1) of Presidential decree No. 600/1973. Contra: see Piazza, M. *Guida alla fiscalità internazionale*, Milano, 2004, p. 446, which bases his position upon the otherwise arising double taxation: the first layer of tax being applied on a transparent basis against the partners (or, for that matter, the individual entrepreneur) and the second by way of the withholding tax.
167. Art. 152(2) ITA.
168. Piazza, op. cit., pp.450-452.
169. I.e. at the date of delivery or shipment for movable goods, unless a postponement in the transfer of title or constitution of the right is agreed by the parties; at the date of the agreement for real estate, once again, unless a deferral of the transfer of title or constitution of the right is provided.
170. The percentage of reimbursement was 4/9 until the introduction of Art. 2(6), Law Decree 138 of 13 August 2011, currently under examination by the Parliament for its conversion into law.
171. See the Regulation issued by the Director of the Tax Agency on 28 December 2001.
172. In this sense, see Ministry of Finance, Circular letter 165/E of 1998 and Art. 27(3) and (3ter) of Presidential decree 600/1973. To the contrary, however, see the letter of Arts. 151(2), 153(2) and 152(1) ITA. For further analysis, refer to Uckmar, Corasaniti and de'Capitani, *Manuale di diritto tributario internazionale*, Padova, 2009, Chap. IV, Para. 8.
173. Art. 23(1)(b) ITA, in line with the OECD approach as per Art. 10(2) and (4) of the OECD Model. See, however, the recent decision of the Supreme Court No. 9197/2011, according to which interest received by a foreign bank on an Italian loan outside the scope of activity of its Italian PE (there was actually no PE in Italy in that case) should not be taxed in Italy.
174. Art. 23(1)(f)(1) ITA.
175. Art. 5(5) of Legislative decree 461/1997.
176. Falsitta, G., Fantozzi, A. Marongiu, G. and Moschetti, F., *Commentario breve alle leggi tributarie -*

Accertamento e sanzioni, Vol. II, Padova, 2011, sub Art. 27ter (Corasaniti, G.).

177. Italian Tax Agency, Circular letter No. 165/E of 1998, Para. 4.11.
178. Art. 12(13) Legislative decree 461/1997; Ministerial decree 4 February 1998.
179. Such percentage has been reduced to 10% as of 1 January 2009 based on Legislative decree 6 February 2007, No. 49, implementing Directive 123/2003/EC.
180. Piazza, M., op. cit., p. 455.
181. *Assonime*, Circular letter No. 63/1994, p. 10.
182. Italian Tax Agency, Ruling No. 93/E of 2007.
183. Piazza, M., op. cit., p. 457.
184. *Assonime*, Circular letter 63/1994; Maisto, G., *Il regime tributario dei dividendi nei rapporti tra società madri e società figlie*, Milano, 1996, p. 138. More recently, see Menti, F., *l'imposizione degli utili da partecipazione societaria*, Padova, 2007, p. 135 et seq.
185. Italian Tax Agency, Rulings 8 October 1999, No. 153/E and 13 March 2006, No. 37/E.
186. The vastly predominant literature has stated that liquidation proceeds must be granted the exemption from withholding tax; see Helminen, M., "Dividend equivalent benefits and the concept of profit distribution of the EC Parent-Subsidiary Directive", *EC Tax Review* 3 (2000) pp. 170-171; De Hosson, F.C. (ed.), *The Direct Investment Tax Initiatives of the European Community*, Kluwer, 1990; Terra, B.J.M. and Wattel, P.J., *European Tax Law*, Kluwer, 1997, p. 355; Vanistendael, F., "The Implementation of the Parent/Subsidiary Directive in the EC - Comments on Some Unresolved Questions", *Tax Notes Int'l* (1992) pp. 605-606; Piazza, M., *Guida alla fiscalità internazionale*, op. cit., p. 464; Giaconia, M. and Ricciardi, M., "La liquidazione volontaria delle società di capitali", *Corriere Tributario* 30 (2000) 2160; Breuninger, G., "Germany", in *The Parent Subsidiary Directive and International Tax Planning*, Amsterdam, 1992, Chap. 4, p. 55; Kellersmann, D. and Treisch, C., *Europäische Unternehmensbesteuerung*, Wiesbaden, 2002, p. 219; Kessler, W. and Spengel, C., DB 2004, Beilage Nr. 6 zu Heft 43, p. 1 et seq. and p. 4; Bullinger, M., IStR 2004, p. 406 et seq., at p. 410, note 26). These authors that favour the exclusion of liquidation proceeds from the exemption recall that the aim of the exemption is to favour the consolidation of European groups at a Continental level, while a liquidation contradicts such spirit. It seems useless, however, to deny the benefits of the Directive in case of liquidation when the same amounts could be easily distributed before liquidating the company and thereby enjoy the exemption from withholding tax at source.
187. In this sense Maisto, op. cit., p. 303 et seq.; in the sense that control under Art. 2359 CC must exist, Amyas d'Aniello, F., "Il regime fiscale delle holding europee", *Rivista di diritto tributario internazionale*, 1 (2000) p. 198.
188. The ECJ has clarified that the holding of shares and financial instruments by a holding company may qualify as a business activity, also for VAT purposes, any time the holding company actually manages such assets and intervenes in the management of the participated companies through the "involvement in the management of the companies in which the holding has been acquired, without prejudice to the rights held by the holding company as shareholder" (ECJ, 20 June 1991, Case C-60/90, *Polysar Investments BV v. Inspecteur der Invoerrechten en Accijnzen*, *Racc.* 1991, p. I-3111; see also ECJ, 20 June 1996, Case C-155/94, *Wellcome trust Ltd v. Commissioners of Customs and Excise*, *Racc.*, 1996, p. I-3013 and *Rivista di diritto finanziario e scienza delle finanze*, (1998) II 3, with comment of Monaco, C., "Le attività finanziarie tra esenzione ed esclusione nella disciplina Iva: l'interpretazione della Corte di Giustizia Ce".
189. Italian Tax agency, Circular letter, No. 60/E of 2001 and Ruling No. 109/E of 2005.
190. Ministry of Finance, Circular letter 6 November 1998, No. 288/E.
191. Ministry of Finance, Circular letters 11 November 1981, No. 36 and 26 June 1986, No. 104.
192. ECJ, 17 October 1996, Case C-283/94 and Case C-291/94, *Denkavit*.
193. Art. 38(2) Presidential decree 602/1973.
194. As said above, indeed, Art. 44(2)(a) imposes a tax treatment equal to the treatment of shares for certain securities whose remuneration fulfils the requirements explained above at 17.2. Contracts are not treated like shares, with the exception of what is provided under Arts. 109(9) and 44(1)(f) ITA concerning silent partnerships where the contribution of the silent partner is not made in works or services (see above at 17.2.).

195. With regard to inbound dividends, however, a possible violation of EU law might be envisaged in respect of individual portfolio investors subject to the substitutive tax of 12.5% (20% as of 1 January 2012) on the dividend received net of foreign taxes, as in this case they are denied the credit for foreign withholding taxes and actually incur double taxation; see above for a more detailed description of the issue.
196. This statement was correctly based on ECJ case law: 14 December 2006, Case C-170/05 *Denkavit international*; 8 November 2007, Case C-379/05 *Amurta*; see also the decision of the EFTA Court 8 November 2004, E-1/04 *Fokus Bank ASA*.
197. ECJ, 19 November 2009, Case C-540/07, *Commission v. Italy*.
198. The action was based on the freedom of movement of capital granted by Art. 56 of the treaty because participations not entailing the power to be actively involved in the management of the company were under focus.
199. The provision is subject to further challenges of discrimination in that it does not eliminate prior discriminations perpetrated until the date of entry into force of the new regime: withholding taxes applied in excess of the 1.375% upon corporate taxpayers subject to tax and resident in an EU or EESA country that exchanges information with the Italian tax authorities must be reimbursed based on the decision of the ECJ in Case C-540/07, mentioned above.
200. The levy of 1.375% results from the taxation of 5% of the dividend under the nominal corporate tax rate of 27.5%. For additional considerations, see Italian Tax Agency, Circular letter No. 26/E of 2009.
201. Art. 27(3^{ter}) of Presidential Decree No. 600/1973.
202. Art. 27(3) Presidential Decree 600/1973.
203. The proceedings were closed on 18 March 2010 because Italy had meanwhile changed its legislation.
204. According to which, "A company resident in France, mentioned in paragraph 2(a), or liable to the French law applicable to parent companies, which receives dividends from a company resident in Italy which would entitle a resident of Italy receiving such dividends to a tax credit (*credito d'imposta*), is entitled to a payment from the Italian Treasury equal to half of such tax credit, reduced by the withholding at source at the rate provided in paragraph 2".
205. Supreme Court, 15 April, No. 8621, *Boll. Trib.* (2011) p. 1482.
206. This part of the decision has been criticized in the literature; see Morri, S. and Bernini, S., "Maggiorazione di conguaglio e dividendi: ritenute asimmetriche?", *Fiscalità internazionale* 3 (2005) p. 239.
207. See 17.2. above.
208. In this sense, see also Art. 44(1)(e) ITA.
209. Piazza, op. cit., p. 519.
210. Art. 23(1)(d) ITA affirms the Italian power to tax self-employment income of non-residents only in case the activity is conducted in Italy.
211. See 17.1. and 17.2. above.
212. Art. 2346(4) CC.
213. Art. 2350(1) CC.
214. Art. 2348(2) CC.
215. Art. 2350(2) CC.
216. Art. 2437^{sexies} CC.
217. Art. 2468 CC.
218. As regards the notion of "risks", see Para. 25 of the Commentary to Art. 10.
219. Especially if such bonds are issued by companies admitted to trading on an Italian regulated market, banks or securitization conduit companies which benefit from the exemption of Arts. 6 and 7 of Legislative Decree No. 239 of 1996 for those receivers who are resident in countries that provide for the exchange of information (white-list countries).

220. Piazza, op. cit., p. 520.
221. Id., p. 521.
222. Id., pp. 521-522.
223. Id., p. 522.
224. Id.
225. See Escalar, G., "Il nuovo regime di tassazione degli utili da partecipazione e dei proventi equiparati nel decreto legislativo di riforma dell'imposizione sui redditi", *Rassegna tributaria* 6 (2003) p. 1956; Assonime, Circular letter No. 32 of 14 July 2004, pp. 29 and 30, quoted by Piazza, op. cit., p. 522.
226. Piazza, id.
227. See Art. 1(3) of the UCITS IV Directive 2009/65/EC, in line with the previous wording of Directive 85/611/EEC, according to which: "The undertakings referred to in paragraph 2 may be constituted in accordance with contract law (as common funds managed by management companies), trust law (as unit trusts), or statute (as investment companies)."
228. CONSOB, *Comunicazione DIN/2049128 del 15 luglio 2002*.
229. Art. 1(1)(f) of the Finance Code (*Testo Unico della Finanza*), Legislative Decree 24 February 1998, No. 58, as modified by Art. 32 of Law Decree No. 78 of 1 July 2009.
230. ABI, Opinion No. 832 11 June 2003. See also heading 10 of the Regulation of the Italian Stock Exchange, concerning collective investment funds.
231. See., Circular letter of 18 August 2009 of the *Bundesministerium der Finanzen*.
232. Circular letter No. 33/E of 15 July 2011.
233. Ruling No. 137/E of 4 October 2005.
234. Supreme Court, decision No. 10990 of 14 July 2003.
235. Gaiani, L., "Thin capitalization: tassazione degli interessi attivi per i soci non residenti", *Contabilità finanza e controllo*, 6 (2004) p. 575, as quoted by Piazza, op. cit., p. 523.
236. Bracco, P., "Tax Treaties and Tax Avoidance: Application of Anti-Avoidance Provisions - Italy", *IFA Cahiers*, 2010, Vol. 95a, pp. 427-447.
237. In this respect, see Uckmar, V., "General Report", in IFA, *Tax Avoidance/Tax Evasion, Cahiers de droit fiscal international*, Vol. 68a, Deventer-Boston, 1983, p. 46; "Le convenzioni contro le doppie imposizioni con riguardo all'America latina", *Dir. prat. trib.*, 1 (1996) p. 1196; Uckmar, V., "I trattati internazionali in materia tributaria", in AA.VV., *Corso di diritto tributario internazionale*, Padova, 2005; Lovisolo, A., "Elusione ed evasione fiscale nei rapporti internazionali", *Dir. prat. trib.*, 1 (1985) p. 1198; Pistone, P., "l'abuso delle convenzioni internazionali in materia fiscale", in AA.VV., *Corso di diritto tributario internazionale*, Padova, 2005. For an analysis on the specific topic of anti-abuse measures in the double tax conventions signed by Italy, see Valente, P. and Magenta, M., "Analyses of certain anti-abuse clauses in the tax treaties concluded by Italy", *International Bulletin for Fiscal Documentation* (2000) pp. 41-46.
238. Rosenbloom, H.D., "Review: OECD Report 'Double Taxation Conventions and the Use of Conduit Companies'", *Intertax* (1988) p. 179.
239. Italy-United States Income Tax Treaty, entered into force on 16 December 2009. In particular, Art. 2 of the Protocol contains an LOB provision, which is, as recalled by the same Art. 2 of the Technical Explanations, "substantially similar" to Art. 22 of the US Model Treaty.
240. Similarly, Italy-Kazakhstan double tax convention of 22 September 1994.
241. See the ECJ decisions in *Open Skies*, 5 November 2002, Cases C-466/98, C-467/98, C-468/98, C-469/98, C-471/98, C-472/98, C-475/98 and C-476/98; Mason, R., "U.S. Tax Treaty Policy and the European Court of Justice", *Dir. prat. trib. int.* 1 (2007) p. 57 (the cases concerned aviation, not taxation).
242. ECJ, 12 December 2006, Case C-374/04, *Test Claimants in the IV ACT Litigation Group*; O'Shea, T., "Netherlands-U.S. Air Transport Agreement Won't Fly, Says ECJ", *Tax Notes Int'l* (2007) p. 790.
243. For the Italian literature, see, among others, Ballancin, A., "La 'nozione di beneficiario effettivo'

- nelle Convenzioni internazionali e nell'ordinamento tributario italiano", *Rassegna tributaria* 1 (2006) p. 209; Montesano, P., "Brevi note sulla qualifica del soggetto come 'beneficiario effettivo' prevista dal Modello di convenzione OCSE", *Bollettino tributario* 3 (2008); Perrone, C., "Brevi note sul significato convenzionale del concetto di beneficiario effettivo", *Rassegna tributaria* 1 (2003) p. 151; Lovisolo, A., "Possesso di reddito ed interposizione di persona", *Diritto e pratica tributaria* 1 (1993).
244. OECD, *Clarification of the meaning of "beneficial owner" in the OECD Model Tax Convention-Discussion Draft* (2011).
 245. OECD, Committee on Fiscal Affairs, "International tax avoidance and evasion: Four related studies", Paris, 1987.
 246. Para. 2 of the Commentary to Art. 10 of the OECD Model.
 247. OECD Committee on Fiscal Affairs on "Double Taxation Conventions and the Use of Conduit Companies", Paris, 1987.
 248. OECD, *Discussion draft - Clarification of the meaning of "beneficial owner" in the OECD Model Tax Convention*, 29 April 2011.
 249. In line with the OECD approach, Ministry of Finance, Ruling No. 12/431 of 7 May 1987.
 250. For an analysis of the different opinions see, among others, Du Toit, C., "Beneficial Ownership of Royalties", *Bilateral Tax Treaties*, Amsterdam, 1999; Vogel, K., *On Double Taxation Conventions*, London-The Hague-Boston, 1997; Van Weeghel, S., in Oliver, J.D.B., Libin, J.B., Van Weeghel, S. and Du Toit, C., "Beneficial Ownership", *Bulletin for International Fiscal Documentation* (2000) p. 321; Libin, J.B. in Oliver et al., id., p. 322.
 251. Vogel, K., *On Double Taxation Conventions*, 3rd ed., London-The Hague-Boston, 1997; Oliver J.D.B. id., p. 310. See also IFA seminar, "The OECD Model Convention - 1998 and beyond, The Concept of Beneficial Ownership", *Tax Treaties*, l'Aia-Boston, 2000.
 252. See Tax Court of First Instance of l'Aquila (*Commissione tributaria provinciale di l'Aquila*), 22 January 2008, No. 1; Tax Court of First Instance of Turin (*Commissione tributaria provinciale di Torino*), 19 October 2010, No. 124, according to which the absence of the entrepreneurial risk, the reduced operative structure and the full control of the recipient of the royalties by a single (Bermuda-based) company indicate that the recipient is only a formal one and not the real beneficiary.
 253. The most recent and authoritative precedent is the decision of the Supreme Court No. 4600/2009. In this case, a Japanese investment fund had assigned some assets to a Japanese bank, which in turn had invested - via a US partnership - in shares issued by Italian companies. The US partnership was fiscally transparent and the dividends paid to it were actually attributed for tax purposes, both in the United States and in Japan, to the Japanese pension fund. Nonetheless, based on the mere wording of Art. 10 of the convention between Italy and Japan, signed in 1969, the Court rejected the request of reimbursement filed by the Japanese fund because the payment had been made to the US partnership and Art. 10 of the convention (like the 1963 version of the OECD Model) refers to "dividends paid to". The Court thus overlooked the current OECD approach and all clarifications that have been inserted in the Commentary over time (in particular in 2003, see above) ever since the introduction of the beneficial ownership clause in the 1977 version of the Model; no explicit reference was made to the fact that the convention was signed before the introduction of the beneficial ownership clause in the Model in 1977. Incidentally, the Court also stated that the bank, and not the pension fund, should be considered as the beneficial owner of the dividends, as income received from the fund was the result of the management activities of the bank, not of the indirect participation into the distributing companies.
 254. Corasaniti, G., "Dividendi, interessi canonici e plusvalenze nel modello Ocse", in Uckmar, V. (ed.), *Corso di diritto tributario internazionale*, Padova, 2005, p. 487; Perrone, "Brevi note sul significato convenzionale del concetto di beneficiario effettivo", op. cit.; Contrino, A., "La convenzione tra l'Italia e la Svizzera contro le doppie imposizioni", in AA.VV., *Le convenzioni dell'Italia in materia di imposte su reddito e patrimonio*, Milano, 2002, p. 956; Bagnardi, B., "Il concetto di beneficiario effettivo nella direttiva sulla tassazione del risparmio", *Dir. prat. trib. int.* (2003) p. 185; Ballancin, A., op. cit.
 255. See also, Italian Tax Agency, Circular letter No. 47/E of 2005, according to which, in order to be qualified as "beneficial owner", it is required that "the recipient of the interests and royalties benefits from the operation.... Therefore, in the light of the anti-abuse scope of the provision, it is believed that the company should be considered as the beneficial owner if it has the ownership and control over the perceived income."

256. Circular letter No. 47/E of 2005.
257. Ruling No. 167/E of 2008, op. cit.; see also de'Capitani, P., "l'applicazione delle ritenute in uscita sui dividendi in tre sentenze della CTP di Pescara", *Dir. Prat. Trib. Int.* 1 (2010) p. 537.
258. In this sense, see also Ministry of Finance, Resolution No. 167/E of 2008; Circular letter No. 306 of 1996.
259. Art. 10(3)(b) and (c) and Art. 10(4)(a) and (b) of the Italy-United Kingdom treaty (21 October 1988).
260. In respect of such clauses, see Maisto, G., *Elusione e abuso del diritto tributario*, Milano, 2009.
261. *Corte di Cassazione*, decisions No. 30055, 30057, 30058 of 23 December 2008.
262. Maisto, G., "Italy - Italian Anti-Avoidance Rules and Tax Treaties", *Bulletin for International Taxation*, 8/9 (2010). See in particular, Paras. 9.2 and 22.1. of the Commentary on Art. 1 of the OECD Model.
263. Legislative Decree No. 143/2005 has implemented Directive 2003/49/EC on a common system of taxation applicable to interest and royalty payments made between associated enterprises.
264. See Fransoni, G., "Abuso di diritto, elusione e simulazione: rapporti e distinzioni", in *Corr. Trib.* 1 (2011); Beghin, M., "La Cassazione prosegue nella 'cesellatura' della nozione di abuso del diritto", *Corr. Trib.* (2010) p. 1347; de'Capitani, P., "La spettanza del credito per le imposte estere e la indeducibilità dei *manufactured payments* in una decisione della Commissione tributaria provinciale di Reggio Emilia a cavallo tra elusione ed evasione tributaria", to be published.
265. See previous note.
266. Art. 29 of the treaty between Italy and Argentina (1979). Similar wording can be found in the treaties signed by Italy with, among others, Austria, Belgium, Brazil, Canada, the United Kingdom, Greece, Israel, Kazakhstan, Luxembourg, Malaysia, Spain, Portugal, the United States, South Africa and Switzerland.
267. Lang, M., "The Procedural Conditions for the Implementation of Tax Treaty Obligations Under Domestic Law", *Intertax* (2007) pp. 146-151.
268. Art. 35 of Presidential decree No. 602/1973; Italian Tax Agency, Ruling No. 183/E of 24 September 2003. *Assonime*, Circular letter 119 of 20 July 1981.
269. See Piazza, op. cit., pp. 1017-1022 for a specific description.
270. Ministry of Finance, Ruling No. 2/12/063 of 4 February 1980; Circular letter No. 7 of 25 March 1981; Ruling No. 12/260 of 10 June 1989; Circular letter No. 23 of 13 August 1992; Ruling No. 99/E of 30 April 1997; see Piazza, op. cit., p. 1023.
271. See also Ruling No. 68/E of 24 May 2000; Ruling. No. 104/E of 6 May 1997; Circular letter No. 306/E of 1996.
272. See the conventions with Switzerland and France.
273. Italian Tax Agency, Ruling No. 37/E of 13 March 2006.
274. See Piazza, op. cit., p. 1034.
275. See supra under 17.6.1. for the same aspects concerning the Parent-Subsidiary Directive.
276. Art. 38, Presidential decree No. 602/1973, which is applicable given that the treaties usually leave these issues to the rules provided by the country where the refund must be requested.
277. See Order of the Director of the Italian Tax Agency of 28 December 2001.
278. According to Art. 10(4)(b), the French shareholder "is entitled to a payment from the Italian Treasury equal to half of such tax credit" (emphasis added).
279. According to Art. 10(4)(b), the UK shareholder is "entitled to a tax credit equal to one half of the tax credit to which an individual resident in Italy would have been entitled had he received those dividends" (emphasis added).
280. *Corte di Cassazione*, 4 May 2004 No. 8450 and 10 June 2004, No. 11033. For a comment, see Della Valle, E. and Marini, G., "Restituzione del credito d'imposta sui dividendi di fonte pattizia", *Corr. trib.* (2004) p. 2455; Bruzzone, M., "Differenti termini per il 'pagamento' di fonte convenzionale del credito d'imposta sui dividendi", *GT-Riv. giur. trib* (2004) p. 926. See also *Corte di Cassazione*, 5 May 2003, No. 25947 and, more recently, *Corte di Cassazione*, 29 October

2008, No. 25947.

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