



Italian Supreme Court refers to the CJEU's Danish cases to interpret the requirement of beneficial owner under the Interest and Royalty Directive (decision No. 14756 of 10 July 2020)

On 10 July 2020, the Italian Supreme Court issued its decision No. 14756 in which, amongst others, interpreted the requirement of beneficial owner in the context of the Interest and Royalty Directive (Directive 2003/49/EC; "IRD").

The case concerned interest paid by an Italian company to its controlling shareholder, a Luxembourg sub-holding ("LuxCo") carrying on financial and treasury functions. The interest accrued on a loan granted in the context of a broader MLBO transaction, put in place for the purpose of acquiring target companies in Italy and Sweden.

The Italian tax authorities claimed that the withholding tax exemption, provided for in Article 26-*quater* of the Presidential Decree 29 September 1973, No. 600, which implemented the IRD in Italy, was not applicable as the Luxembourg sub-holding had to be regarded as a conduit company and, therefore, not as the beneficial owner of the interest payments. According to the Italian tax authorities the conduit role of LuxCo resulted from the following circumstances: (i) the fact that it carried out only holding functions; (ii) the existence of loans between LuxCo and the Italian company with conditions similar to those of the loan granted to LuxCo by its controlling shareholder; (iii) the fact that LuxCo transferred to the controlling shareholder the interest it received from the Italian company after a short period of time and that it only derived a reduced markup of 0.125%.

The Supreme Court upheld the decision of the Court of Appeals that the Luxembourg sub-holding had to be regarded as beneficial owner of the interest.

The Court based to a large extent its decision on the judgment issued by the Court of Justice of the European Union ("CJEU") on 26 February 2019 in the joined cases C-115/16, C-118/16, C-119/16 and C-299/16, dealing with the application of the IRD ("Danish cases"). In particular:

- it stressed that the direct recipient of the interest is not the "beneficial owner" when that recipient's right to use and enjoy the interest is constrained by a contractual or legal obligation (which may result either from a legal document, or from the actual behaviours of the parties) to pass on the income received to another person;
- it emphasized the relevance of the OECD Commentary on Article 11 for the purpose of interpreting the requirement of "beneficial owner" in the context of the IRD;
- it referred to the notion and *indicia* of tax abuse (and related burden of proof) provided in paragraphs 124, 130, 131 and 145 of the Danish cases (see EU TAX ALERT 2019/03 at <https://maisto.it/en/newsletter/eu-tax-alert--64.html>).

In addition the Supreme Court recalled its prior case law (in particular, decision No. 27116 of 28 December 2016), where, in the context of the Parent Subsidiary Directive (Directive 2011/96/EU of 30 November 2011; "PSD"), it held that the assessment of the "beneficial owner" requirement should be based on the analysis of the autonomy of the recipient company both in taking the strategic and management decisions related to the underlying asset and in retaining, investing or transferring to a third company the income received. In that case law, the Supreme Court also clarified that the fact that the income recipient is a pure holding company does not preclude the application of the benefits of the PSD.

Based on the above, the Supreme Court held that the Court of Appeals was not wrong in concluding that LuxCo was the beneficial owner of the interest. In this respect, the Supreme Court highlighted that: (i) the sole fact that LuxCo acted as sub-holding and carried out financial and treasury activity did not entail, *per se*, that it was a conduit company not fulfilling the requirement of beneficial ownership; (ii) there was no contractual, or legal obligation for the recipient to pass on the income received to a third party; (iii) the net profits derived by LuxCo were adequate, having regard to the specific activity carried out; and (iv) the loan granted to the Italian company was only one of the several loans granted to other group companies in the context of the MLBO transaction aimed at acquiring the target companies in Italy and Sweden.

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