MAISTO E ASSOCIATI

**TAX TREATY ALERT 2021/05**

## Italian Supreme Court rules on the interaction between Article 10 of the Italy – France Tax Treaty and the Parent Subsidiary EU Directive

With its order no. 24874 of 15 September 2021, the Italian Supreme Court ("**Supreme Court**") ruled on a case dealing with the distribution of dividends by a French resident subsidiary to its Italian resident parent company ("**ItaCo**"). In particular, the Supreme Court dealt with the interaction between the French dividend tax credit (*avoir fiscal*) that could be partially refunded in the past under the tax treaty between Italy and France ("**Treaty**") and the dividend exemption under Italian law implementing Article 4 of Directive 90/435/EEC of 23 July 1990 (the Parent Subsidiary Directive, now Directive 2011/*96*/EU of 30 November 2011; "**Directive**"). Although the *avoir fiscal is no longer available* since 1 January 2006, the Supreme Court decision may still be relevant for similar cases pending before domestic tax courts.

The dispute arose because ItaCo obtained the French dividend tax credit under Article 10(3)(b) of the Treaty and at the same time excluded 95% of the dividends from the Italian corporate tax base pursuant to then applicable Article 96-*bis* of Presidential Decree no. 917 of 22 December 1986 (the Italian Income Tax Act).

The Italian Revenue Agency challenged ItaCo's entitlement to the dividend exemption under the Directive, maintaining that the joint application of the two regimes would have resulted in an undue tax benefit, which went beyond the aim of eliminating double taxation. Both the Provincial Tax Court of Venice and the Regional Tax Court of Veneto confirmed the position of the Italian Revenue Agency.

The Supreme Court overruled the decisions of the lower courts and, in doing so, it referred to its previous case law on the reverse situation in which Italian source dividends were paid to UK resident companies (e.g., decision no. 20646 of 20 July 2021).

According to the Supreme Court, the French dividend tax credit provided for by the Treaty does not necessarily eliminate the risk of economic double taxation nor the risk of violation of the principle of fiscal neutrality as interpreted by the Court of Justice of the European Union (Case C-389/18, *Brussels Securities SA v. État Belge*, 19 December 2019). Therefore, ItaCo was considered still entitled to the 95% dividend exemption under the Italian statute implementing the Directive, subject to assessment of the application of the 5% Treaty withholding tax on both the tax credit and the dividends received. This conclusion is consistent with Article 7(2) of the Directive.

The Supreme Court decision is to be welcomed as it correctly interprets the interaction between the Treaty tax credit and the exemption under the Directive. First, the circumstance that Article 10(3)(b) of the Treaty explicitly provides for the refund of half of the French tax credit on dividends paid to Italian shareholders "liable to the Italian law applicable to parent companies" suggests that the two regimes may be applied concurrently. Moreover, there is no provision in the Directive that implies that the Directive does not apply in cases where double taxation is already excluded or mitigated by tax treaty provisions (or the other way around). Rather the contrary, under Article 7(2) of the Directive, the Directive "shall not affect the application of domestic or agreement-based provisions designed to eliminate or lessen economic double taxation", including therefore treaty provisions relating to the attribution of tax credits to the recipients of dividends (like the ones that can indeed be found in Italy's tax treaties with France and the United Kingdom).

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