Italian tax authorities clarify the scope of application of foreign tax credit under tax treaties

In its decision No. 16697 of 21 June 2019, the Supreme Court found a Dutch sub-holding company (hereinafter "**DutchCo**") to be resident of Italy under Article 4(3) of the Italy-Netherlands Income and Capital Tax Treaty (hereinafter the "**DTC**").

The Italian Tax Authorities (hereinafter the "**ITA**") challenged DutchCo, having its legal seat in the Netherlands, to be tax resident of Italy for both domestic and treaty purposes (from 1999 to 2002), arguing that it had therein its place of effective management.

Both the Provincial and the Regional Tax Courts held in favour of the ITA.

The Supreme Court confirmed the judgements of the lower Courts, making reference to some of its previous decisions, as well as to the case law of the Court of Justice of the European Union (hereinafter "**CJEU**") dealing with the EU freedom of establishment and VAT (in particular, Case C-194/06, *Cadbury Schweppes*, of 12 June 2006 and Case C-73/06, *Planzer Luxembourg Sàrl*, of 28 June 2007).

As regards the concept of "place of effective management" under Article 4(3) DTC, the Supreme Court observed that:

- such concept is substantially equivalent to that of "place of management" provided for by domestic tax law in order to establish the tax residence of companies and other entities; and
- both the "place of effective management" under the DTC and the "place of management" under domestic law denote the place where the management and control functions of the company are effectively located and the relevant decisions are taken.

Based on these premises, the Supreme Court held that the Regional Tax Court was correct in deciding that the place of effective management of DutchCo was located in Italy in the relevant tax years, considering that:

- management directives, strategic and operative decisions, as well as investment and expenditure authorisations (even those of unimportant character, e.g. authorisations to enrol in language courses or to incur medical expenses) were taken in Italy by the managers of the Italian controlling company;
- although the meetings of DutchCo's board of directors, which the Italian directors normally did not attend in person, took place in the Netherlands, the decisions formally taken during such meetings were actually discussed and taken in advance in Italy;
- the Amsterdam office was simply the place where the day-to-day business was carried out.

The Supreme Court also found that DutchCo was a mere artificial structure, set up exclusively for tax purposes. In this respect, the Court made reference to the fact that it had only two employees who merely executed directives coming from Italy and that the Amsterdam office was of limited dimensions.

The Supreme Court's decision is somewhat surprising as it seems to downgrade the importance of day-to-day management for the purpose of establishing the tax treaty

residence of a company, thus partially departing from some of the most recent judgements of the same Court (e.g. decisions No. 33234 and No. 33235 of 21 December 2018, where the Supreme Court held that, in order to identify the place of effective management of a company, it is not sufficient to establish where its key decisions are taken, but it is also necessary to determine where its day-to-day management is carried out; *see* our Tax Treaty Alert 2019/02).

Finally, it is worth mentioning that DutchCo requested the Supreme Court to refer a preliminary question to the CJEU with regard to the compatibility of the domestic rule setting the criteria for company tax residence (as interpreted by the Regional Tax Court) with the EU freedom of establishment. The Supreme Court, however, decided without referring any preliminary question to the CJEU, as it considered its interpretation of the concept of "place of management" in line with the case law of the latter Court.

For further information: **Maisto e Associati**

Milan
Piazza F. Meda 5
20121
T: +39.02.776931

Rome
Piazza d'Aracoeli 1
00186
T: +39.06.45441410

London
2, Throgmorton Avenue
EC2N 2DG
T: +44.207.3740299
