2 June 2020

Global Tax Alert

Italian Tax Authorities provide clarifications on Brexit impact on Italian source taxation and application of look-through approach to outbound dividends paid to ACS

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Executive summary

On 28 May 2020, the Italian Revenue Agency (ITA) published Ruling No. 156, which addresses the tax treatment of Italian source dividends paid to an Authorized Contractual Scheme (ACS) established by a pool of United Kingdom (UK) pension funds.

The ITA clarified that no look-through approach can be applied with respect to the Italian 11% withholding tax (WHT) rate that Article 27(3) of Italian Presidential Decree No. 600 of 29 September 1973, (the Decree), provides for European Union (EU)/European Economic Area (EEA) pension funds receiving Italian source dividends.

Consequently, the ITA stated that:

- The ACS is not entitled to the reduced 11% WHT rate, because it is not a pension fund.
- The UK pension funds cannot claim the application of the reduced 11% WHT because they are not the direct recipients of the dividends.

Conversely, a look-through approach can apply for the purposes of the tax treaty benefits, where applicable, to the participants of the ACS.

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Detailed discussion

Background

The ruling query was submitted by the manager (Claimant) of one of the largest UK public pension schemes structured as an ACS, that is a contractual arrangement without distinctive legal personality and transparent for tax purposes. The Claimant asked the ITA to confirm whether: (i) the ACS would be entitled to the application of reduced Italian taxation on outbound dividends paid to EU/EEA pension funds; and (ii) whether treaty benefits could be granted by each treaty entitled pension fund participating in the ACS.

The Ruling

The ITA clarified the following:

- Application of the reduced Italian WHT at 11% rate provided for by Article 27(3) of Italian Presidential Decree No. 600 of 29 September 1973 (the "**Decree**"), to Italian source dividends paid to EU/EEA pension funds, is conditional upon the qualification of the direct recipient as pension fund. Accordingly, no "look-through" approach can be applied.
- Consequently, the ACS, being the direct recipient of the Italian source dividends, does not qualify as a UK pension fund and, therefore, cannot invoke the application of the reduced WHT of 11% rate in lieu of the statutory 26% rate.
- The UK pension funds, not being the direct recipient of the Italian source dividends, are not entitled to the reduced 11% WHT.
- The look-through approach conversely can apply for the purposes of the tax treaty benefits, where applicable, to the participants of the ACS, to the extent that the ACS is regarded as fiscally transparent in the State of residence of its participants.
- With respect to transparency, the Ruling clarified that the such condition is met when the income produced by the ACS is allocated to the pension funds for the purposes of the UK taxation, even if the income is not effectively distributed by the ACS.
- Accordingly, the Ruling supersedes the approach formerly adopted by the ITA with regard to foreign investment vehicles, which was based on the commitment of the foreign investment vehicle to make periodical distributions, at least annually, to its participants.

Incidentally, the Ruling also clarified that the after-Brexit transitional period of 18 months set forth by Decree 22/2019, during which the Italian tax regimes provided for EU residents would have been applicable to UK entities in the event that a no Brexit deal were reached, is no longer applicable, given that the Agreement on the withdrawal of the UK was signed on January 2020.

Consequently, further to the termination of the Brexit transition period (i.e., 31 December 2020), the UK will cease to be considered as an EU Member State and UK citizens will no longer be entitled to the Italian tax regimes provided for resident of EU countries.

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EYG no. 003733-20Gbl

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