Complete Distributive Rules and the Single Tax Principle: A Review of Recent Italian Case Law

Reuven S. Avi-Yonah
University of Michigan Law School, aviyonah@umich.edu
Gianluca Mazzoni
University of Michigan Law School, gmazzoni@umich.edu

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Complete Distributive Rules and the Single Tax Principle: A Review of Recent Italian Case Law

Reuven Avi-Yonah[*]
and Gianluca Mazzoni[**]

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The authors, in this article, examine the application of complete distributive rules as set out in various tax treaties as it relates to the single tax principle by reference to recent Italian case law.

1. Introduction

On 11 October 2018, in Decision No. 25219,[1] the Italian *Corte Suprema di Cassazione* (Supreme Court, CSC) confirmed that treaty provisions limiting the exercise of the domestic power to tax by the source state also apply where the residence state does not actually tax the relevant item of income. In that case, where a tax treaty attributes exclusive tax jurisdiction over an item of income to the residence state, the domestic law of which currently exempts such item of income, double non-taxation arises.

According to the CSC, when the source state waives its power to tax to the benefit of the residence state, it may not recover its original tax jurisdiction. In other words, the waiver by a contracting state of its power to tax does not have to be necessarily correlated with the exercise by the beneficiary state of its right to tax. Double non-taxation arising as a result of an interaction between treaty provisions and domestic law seems to be acceptable as it is consistent with the basic function of a tax treaty, i.e. to restrict the domestic taxing rights.[2]

2. Decision No. 25219 of the SCC

The facts of the dispute are the following. By way of a private agreement of 3 July 1997, registered on 15 July 1997, B. GmbH, a German resident company, with no permanent establishment (PE) in Italy, transferred its entire participation in the capital of C.M. srl to F. L.T. srl for a consideration of ITL 22 billion (GBP 15,156,977.07). The Italian Revenue Agency issued a notice of deficiency for the fiscal year of 1997 where it claimed that the taxpayer did not declare, either in Italy or in Germany, the capital gain realized from the sale of shares of an Italian resident company. The taxpayer appealed against the notice of deficiency to the *Commissione Tributaria Provinciale, Bologna* (Tax Court of First Instance of Bologna, CTPB), which rejected the taxpayer's appeal by way of Decision No. 409 of 2007.[3] The taxpayer appealed against this decision to the *Commissione Tributaria Regionale, Bologna* (Regional Tax Commission of Emilia Romagna, CTRB), but again its claims were rejected in a decision of 20 September 2010.[4] As the taxpayer did not register the capital gain in its accounting statements and did not declare it either in Italy or in Germany as resulting from the exchange of information with the German tax authorities, the CTRB argued that the Germany-Italy Income and Capital Tax Treaty (1989)[5] was inapplicable, as no double taxation arose. Therefore, the capital gain should have been subject to tax in Italy as a consequence of the application of articles 23 and 112 of the Italian *Testo Unico Delle Imposte Sui Redditi* (Consolidated Tax Report, TUIR).[6]

As stated in section 1. , the CSC overturned the decisions of both the CTPB and the CTRB by arguing that Italy was prevented from taxing the capital gain by article 13(4) of the Germany-Italy Income and Capital Tax Treaty (1989), which provides that:

> gains from the alienation of any property other than that referred to in paragraphs 1 (immovable property), 2 (movable property of a PE), 3 (ships or aircraft) shall be taxable only in the Contracting State of which the alienator is a resident.

According to the CSC, the fact that B. GmbH did not remit taxes in Germany on the capital gain realized on the sale of shares of C.M. srl did not constitute a valid reason to preclude the application of treaty provisions on the distribution of taxing rights. Rather, it allowed the competent authorities of a contracting state to request information from the other contracting state in order to correctly apply treaty provisions and tackle situations of tax evasion as provided by article 27 of the Germany-Italy Income and Capital Tax Treaty (1989).

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* Irwin I. Cohn Professor of Law, University of Michigan. The author can be contacted at: aviyonah@umich.edu .
** SJD candidate, University of Michigan. The author can be contacted at: gmazzoni@umich.edu .
1. IT: CSC, 11 Oct. 2018, Decision No. 25219.
2. A. Scapa & L.A. Henie, *Avoidance of Double Non-Taxation under the OECD Model Tax Convention* , 33 Intertax 6/7, p. 267 (2005).
3. IT: CTPB, 12 Dec. 2007, Decision No. 409 of 2007.
4. IT: CTRB, 20 Sept. 2010.
5. *Convention between the Federal Republic of Germany and the Italian Republic for the Avoidance of Double Taxation with Respect to Taxes on Income and on Capital and for the Prevention of Fiscal Evasion* (unofficial translation) (18 Oct. 1989), Treaties IBFD.
6. IT: *Testo Unico Delle Imposte Sui Redditi* (Income Tax Code, TUIR), arts. 23 and 112.

This was without prejudice to Germany, which, as the residence state, had exclusive tax jurisdiction over the capital gain as provided by article 13(4) of that tax treaty.

As mentioned in section 1., in this situation, the taxpayer benefitted from a double exemption because Italy, as the source state, did not tax the income on the basis of the tax treaty, i.e. according to article 13(4) of the Germany-Italy Income and Capital Tax Treaty (1989), and Germany, as the residence state, exempted the capital gain on the basis of its domestic law. According to section 8b(2) of the German *Körperschaftsteuergesetz* (Corporate Income Tax Law, KStG),[7]capital gains on the sale of shares in a non-resident company are exempt from corporate income tax for a resident shareholder.[8]

3. Analysis of Previous Case Law on this Theme

This decision is in line with previous case law of the CSC, in particular with Decision No. 1231 of 29 January 2001,[9]which dealt with a partial refund claim for taxes withheld on outbound dividend distribution from an Italian resident company to a non-resident company. On 21 September 1990, *Foundation de Prévoyance en faveur du personnel de Digital Equipment Corp. SA & des Sociétés affiliées*, a Swiss resident taxpayer, filed a claim for partial refund of ITL 4,231,680, which was equal to the higher rate of taxes withheld on dividends. The taxpayer claimed that it had received from Fiat s.p.a., an Italian resident company, in which it held a participation interest, after the approval of the 1988 balance sheet, dividends in the amount of ITL 24,320,000 on which the domestic withholding rate of 32.4% was applied instead of the reduced treaty withholding rate of 15% as provided for under article 10(2) of the Italy-Switzerland Income and Capital Tax Treaty (1976).[10]The Italian Revenue Agency denied the taxpayer's refund claim, arguing that the Swiss bank affidavit, which stated that the dividends would be deposited on its account, did not satisfy the burden of proof. Both the Provincial Tax Commission and the Regional Tax Commission ruled in favour of the taxpayer. The Regional Tax Commission of Piedmont, in its decision of 11 June 1997, referring to the Provincial Tax Commission's decision, held that the taxpayer had provided enough evidence to the effect that it was entitled to the treaty rate and, therefore, allowed the refund of taxes withheld in excess of 15%. As a consequence, the Italian Revenue Agency appealed to the CSC, arguing that that taxpayer was required to prove that it actually received the dividends and paid taxes thereon in Switzerland. In particular, according to the Italian Revenue Agency, in order to benefit from the reduced treaty withholding rate, the taxpayer was required to submit an official statement from the Swiss competent authorities to the effect that it actually paid taxes on dividends received in Switzerland. In this regard, the Swiss bank affidavit provided by the taxpayer was considered to be insufficient evidence by the Italian Revenue Agency.

The CSC noted that its previous case law on the subject was divided between two different theories. On the one hand, according to the first theory (i.e. subjective tax liability),[11]the reduced treaty withholding tax rate applies if the distributed dividends are liable to tax in the recipient resident state, regardless of whether any tax is actually imposed by that state. On the other hand, according to the second theory (i.e. objective tax liability),[12]the treaty withholding tax rate applies on the condition that the recipient has actually received the dividends and paid taxes thereon in its residence state. In the present case, the CSC decided to follow the first theory as being more consistent with the spirit and purposes of the Italy-Switzerland Income and Capital Tax Treaty (1976). The CSC observed that both article 10 of the Italy-United States Income Tax Treaty (1999)[13]and of the Italy-Switzerland Income and Capital Tax Treaty (1976)[14]are similar,

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7. DE: *Körperschaftsteuergesetz* (Corporate Income Tax Law, KStG), sec. 8b(2).
8. A. Perdelwitz, *Germany – Corporate Taxation* sec. 7., Country Analyses IBFD (accessed 7 Jan. 2019) and R. Martini & T. Weimar, *Germany*, in *Taxation of Companies on Capital Gains on Shares under Domestic Law, EU Law and Tax Treaties* sec. 17.6.1. (G. Maisto ed., IBFD 2013), Online Books IBFD, where it is stated that: "As regards the taxation of actually realized capital gains on shares, *the tax exemption of section 8b(2) of the KStG* is perfectly neutral. It *neither distinguishes* between resident and non-resident taxpayers nor *between shares in domestic and foreign companies*." (Emphasis added.)
9. IT: CSC, 29 Jan. 2001, Decision No. 1231, Tax Treaty Case Law IBFD. *See also* IT: CSC, 21 Feb. 2001, Decision No. 2532, Tax Treaty Case Law IBFD, with regard to which it has been said that: "The Supreme Court … stated that under Art. 10(2) of the treaty, in accordance with the OECD Model, the *taxpayer was not required to prove the payment of taxes in its State of residence* (as required under Italian domestic law to get the refund of the taxes paid in the residence State of the recipient) and so the refund had to be granted)" (emphasis added); IT: CSC, 19 Jan. 2009, Decision No. 1138, Tax Treaty Case Law IBFD, in respect of which it has been stated that: "The Supreme Court then observed that the *treaty prevails over domestic law under Art. 117 of the Italian Constitution* and that, since double tax treaties eliminate double taxation by means of the attribution of taxing rights solely to one of the two contracting states, it was necessary to ascertain whether the right to tax the specific item of income was assigned to Italy or Ireland" (emphasis added) – *see* CSC, 19 Jan. 2009, Decision No. 1138, Tax Treaty Case Law IBFD; and IT: CSC, 18 Nov. 2011, Decision No. 24246, Tax Treaty Case Law IBFD, regarding which it has been said that: "The Supreme Court then noted that article 10(2) of the treaty provides for a shared taxation right which allows Italy to levy a withholding tax of 15% on dividends paid to an individual resident of Switzerland. *This withholding rate applies irrespective of whether the dividends are actually taxed in Switzerland. This is in conformity with the provisions of article 75 of Presidential Decree 600 of 1973, under which international agreements prevail over domestic rules*" (emphasis added) – *see* CSC, 18 Nov. 2011, Decision No. 24246, Tax Treaty Case Law IBFD.
10. *Convention between the Swiss Confederation and the Italian Republic for the Avoidance of Double Taxation and the Regulation of Certain Other Questions Relating to Taxes on Income and Capital* (unofficial translation) (9 Mar. 1976) (as amended through 1978), Treaties IBFD [hereinafter *Italy-Switz. Income and Capital Tax Treaty* (1976)].
11. *See* IT: CSC, 10 Nov. 1999, Decision No. 12458, Tax Treaty Case Law IBFD, in respect of which it has been stated that: "the Supreme Court has recently ruled (repeatedly changing its position) in connection with a particular profile connected to the notion of the beneficial owner, and pertaining to the remarks surfaced in paragraph 54 of the OECD Report about 'application of the OECD Model Tax Convention to Partnerships'. Said profile concerns the possibility to subordinate the implementation of the (normally) more favorable withholding tax, provided by the tax treaties for the taxation of income paid to the beneficial owner, to the circumstance that said subject is taxed in the State of Residence. Of notice, the Supreme Court has stated in the first instance that the DTC's regulations (in this case Art. 10 of the Italy-U.S.A. DTC) must be interpreted to mean that the lower rate was applicable only because of the submission of the dividend to the taxation power of the other State, regardless of the actual payment of the tax."
12. *See* IT: CSC, 9 Mar. 2000, Decision No. 3861, Tax Treaty Case Law IBFD and IT: CSC, 11 Apr. 2000, Decision No. 4560, where, in respect of both cases, it has been said that: "Subsequently, the Supreme Court has changed its opinion and stated that, under Art. 27 d.P.R. n. 600 dated 1973, the proof of the payment of dividends and the compliance with the tax obligations in the State of Residence of the recipient, do constitute the presupposition for the application of the lower DTC rate."
13. *Convention between the Government of the United States of America and the Government of the Italian Republic for the Avoidance of Double Taxation with Respect to Taxes on Income and the Prevention of Fraud or Fiscal Evasion* art. 10(2) (25 Aug. 1999), Treaties IBFD reads:

as they are based on the OECD Model.[15] Finally, the CSC held that the aim of bilateral tax treaties is to avoid conflicts deriving from the overlapping of domestic tax systems by attributing the exclusive taxing right to a contracting state (i.e. the residence state), coupled with the corresponding waiver of the taxing right by the other contracting state (i.e. the source state).[16] In some cases, the residence state of the paying corporation (i.e. the source state) retains a limited taxing right (in the present case at a rate not exceeding 15% on the outbound dividends). The CSC held that such a limited right to tax dividends is exercised in the source state when the recipient of the income is liable to tax in its residence state, regardless of whether any tax is actually paid there.[17] In the present case, the taxpayer, by submitting the affidavit from the Swiss bank, has demonstrated that it is entitled to treaty benefits.

It should be mentioned that Decision No. 1231 of 29 January 2001 was also quoted recently by the CSC in Decision No. 23984 of 24 November 2016[18] concerning the allocation of taxing rights between France and Italy with regard to the income of an Italian resident artist derived from her singing performance carried out in France in 2004 as provided for by article 17 of the France-Italy Income and Capital Tax Treaty (1989).[19] The issues at stake in that case were whether article 17 of the France-Italy Income and Capital Tax Treaty (1989), read in conjunction with article 24, gave the two states concurrent jurisdiction to impose income tax and what the role of the Commentaries of the OECD Model[20] was in treaty interpretation. The facts of the case are the following. In 2004, Patrizia Ciofi, an Italian resident artist, received income from her singing performance carried out in France. She failed to declare this foreign-source income in her 2004 tax return. The Italian Revenue Agency, after auditing the taxpayer, discovered the income and taxed it. The plaintiff argued that she had already declared that income and paid taxes thereon in France, showing an official statement from the French competent authorities to the Italian Revenue Agency. Nonetheless, the Italian Revenue Agency applied article 17 of the France-Italy Income and Capital Tax Treaty (1989),[21] according to which, based on the interpretation given by the tax administration, the fact that the artist had already paid taxes in France did not prevent Italy from taxing that foreign source income, without prejudice to the recognition of the foreign tax credit. The Provincial Tax Commission granted the plaintiff's claim, while the Regional Tax Commission held that the jurisdiction to impose income tax with regard to this situation was not exclusively that of France but, rather, was concurrent. The Regional Tax Commission, based on a circular issued by the tax administration, held that Italy gives up its taxing right only when it is exclusively allocated to the other contracting state. On the other hand, when this is not expressly provided, as in the case at hand, Italy retains its taxing right and the risk of double taxation is mitigated through the recognition of a foreign tax credit for taxes paid abroad. The Regional Tax Commission recognized the plaintiff's good faith and undid the notice of deficiency with regard to sanctions only. Thus, the plaintiff's appeal before the CSC was rejected.[22]

> … However, such dividends may also be taxed in the Contracting State of which the company paying the dividends is a resident and according to the laws of that State, but if the *beneficial owner* of the dividends is a resident of the other Contracting State, the tax so charged shall not exceed
> (a) 5 per cent of the gross amount of the dividends if the beneficial owner is a company which has owned at least 25 per cent of the voting stock of the company paying the dividends for a 12 month period ending on the date the dividend is declared; and
> (b) 15 per cent of the gross amount of the dividends in all other cases. This paragraph shall not affect the taxation of the company in respect of the profits out of which the dividends are paid. (Emphasis added.)

14. Art. 10(2) *Italy-Switz. Income and Capital Tax Treaty* (1976) states that:
> However, such dividends may be taxed in the Contracting State of which the company paying the dividends is a resident, and according to the law of that State; but where the *recipient* of the dividends has a right to their enjoyment the tax so charged shall not exceed 15 per cent of the gross amount of the dividends.
> This paragraph shall not affect the taxation of a company with respect to the profits out of which such dividends are paid.
> The competent authorities of the Contracting States shall agree as to how this paragraph shall be applied. (Emphasis added.)

15. Most recently, *OECD Model Tax Convention on Income and on Capital* (21 Nov. 2017), Models IBFD.
16. "the Supreme Court … has emphasized that such purpose is pursued by the attribution of the power of taxation to a Contracting State and, in the same way, by the waiver or by the limitation of the enforcement of said power by the other State (specifically of the State of Source). Therefore, the Supreme Court has held that the mere existence of the main power of taxation of the other Contracting State (or of the State of Residence) would be consistent with such aims, independently from the effective payment of the tax in that State." *See* A. Pozzo, *Avoidance of Double Non-Taxation in Italy* , in *Avoidance of Double Non-Taxation* Band 26, p. 186 n. 58 (M. Lang ed. 2003).
17. "… In this respect, the CSS has also held that the *OECD Model* does not provide either that the application of a lower rate fixed for the concurrent taxation in the source state should be made conditional on the proof of payment of taxes in the beneficiary's residence state." *See* Pozzo *supra* n. 16 .
18. IT: CSC, 24 Nov. 2016, Decision No. 23984.
19. *Convention between the Government of the French Republic and the Government of the Italian Republic for the Avoidance of Double Taxation with Respect to Taxes on Income and on Capital and for the Prevention of Fiscal Evasion and Fraud (with a Protocol and Exchange of Letters)* (unofficial translation) (5 Oct. 1989), Treaties IBFD [hereinafter *Fr.-Italy Income and Capital Tax Treaty* (1989)].
20. Most recently, *OECD Model Tax Convention on Income and on Capital: Commentaries* (21 Nov. 2017), Models IBFD.
21. Art. 17(1) *Fr.-Italy Income and Capital Tax Treaty* (1989) reads:
> Notwithstanding the provisions of Articles 14 and 15, income derived by a resident of a State as an entertainer, such as a theatre, motion picture, radio or television artist, or a musician, or as an athlete, from his personal activities as such exercised in the other State, *may be taxed* in that other State.
> Where an entertainer or athlete, being a resident of a State, derives income from the other State for performances that have a connection with his professional standing, such income *may be taxed* in that other State.' (Emphasis added.)

22. The CSC in Decision No. 23984 (2016), *supra* n. 18 , with regard to the artist, confirmed the interpretation adopted in the decision and rejected the appeal. In its judgement, the CSC observed that tax treaties, which are usually drawn up on the basis of the *OECD Model* , generally provide either for an exclusive taxing right in respect of the foreign state or for a shared right between the two states. That said, in order to assess whether the provision grants exclusive or shared taxing right, the CSC proceeded to a textual interpretation of art. 17 *Fr.-Italy Income and Capital Tax Treaty* (1989). According to the CSC, the fact that art. 17 merely provides that "income … may be taxed in [the State from which the income originated (the source state)]" is critical. *See* "i Notwithstanding the provisions of Articles 14 and 15, income derived by a resident of a State as an entertainer, such as a theatre, motion picture, radio or television artiste, or a musician, or as an athlete, from his personal activities as such exercised in the other State, may be taxed in that other State." Indeed, the provision, unlike other articles of the Convention tax treaty (such as arts. 15, 18 and 19), does not stipulate that such income may be taxed only in the source state (France in this case), which would be indicative of an exclusive taxing right of the state concerned. Furthermore, art. 17(3) and (4) of the tax treaty uses the word "only" in regulating the case in which performances abroad are funded by public funds of the foreign state, thereby providing for the exclusivity of the taxing right. This means that, under art. 17(1) (which is applicable to the present case), the rights of the two states to tax are to be considered to be shared, as the word "only" does not appear in the text of the provision. In reaching these findings, the CSC expressly relied on the general rule on treaty interpretation as enshrined in *Vienna Convention on the Law of Treaties* art. 31(1) (23 May 1969), Treaties IBFD, which states that: "A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose". Accordingly, it has been stated that:

4. Comments on Decision No. 25219 of the CSC

Returning to the case at hand, i.e. Decision No. 25219 of the CSC, a couple of comments are worth mentioning. First, it appears that such a situation of double non-taxation resulting from the interaction of a treaty provision, in this case article 13(4) of the Germany-Italy Income and Capital Tax Treaty (1989) and German domestic law, i.e. section 8b(2) of the KStG, which provides for exemption of capital gains on the sale of shares in a foreign company, is accepted by both contracting states - Italy and Germany - as being consistent with the basic function of a tax treaty, i.e. to restrict the taxing rights established under domestic laws.[23] Article 13(4) of the Germany-Italy Income and Capital Tax Treaty (1989) is also consistent with the structure of article 13 of the OECD Model. As stated by Reimer[24] both the OECD Model (article 13(5)) and the UN Model[25] (article 13(6)) conclude their capital gains article with a catch-all clause that concerns all capital gains not covered by any of the preceding paragraphs. This clause provides that, where a resident of a contracting state derives gains from the alienation of property other than that referred to in article 13(1), (2), (3) and (4) of both the OECD Model and the UN Model, only the contracting state of which the alienator is resident should remain entitled to tax these gains. In the opinion of Reimer (2015),[26] the sale of shares is primarily governed by the PE principle provided in article 13(2) of the OECD Model and only secondarily by the catch-all clause provided in article 13(5). As mentioned in section 2., B. GmbH did not have a PE in Italy. Therefore, gains from the alienation of shares in companies can only be taxed in the residence state of the alienator (Germany). The source state (Italy) is prevented from taxing such gain, regardless of the level of participation. In this context, the Commentary on Article 13(5) of the OECD Model states that:

> 29 As regards gains from the alienation of any property other than that referred to in paragraphs 1, 2, 3 and 4, paragraph 5 provides that they *are taxable only in the State of which the alienator is a resident*. This corresponds to the rules laid down in Article 22.
>
> 30 The Article does not contain special rules for gains from the alienation of shares in a company (other than shares of a company dealt with in paragraph 4) or of securities, bonds, debentures and the like. *Such gains are, therefore, taxable only in the State of which the alienator is a resident*. (Emphasis added.)[27]

Moreover, the decision of the CSC, according to which, for purposes of the treaty application it is irrelevant whether any tax has been actually levied by the state to which the exclusive tax jurisdiction belongs, is fully consistent with OECD guidance. Indeed, according to the Commentary on Article 4(1) of the OECD Model (2017):

> Paragraph 1 refers to persons who are “liable to tax” in a Contracting State under its laws by reason of various criteria. *In many States, a person is considered liable to comprehensive even if the Contracting State does not in fact impose tax*. For example, charities and other organizations may be exempted from tax, but they are exempt only if they meet all of the requirements for exemption specified in the tax laws. They are, thus, subject to the tax laws of a Contracting State. Furthermore, if they do not meet the standards specified, they are also required to pay tax. Most States would view such entities as residents for purposes of the Convention (*see*, for example, paragraph 1 of Article 10 and paragraph 5 of Article 11). (Emphasis added.)[28]

In this regard, Ismer and Riemer (2015) have argued that:

> States disagree on the question whether persons can be considered “liable to tax” and, thus, residents even though they do *not actually have to pay taxes*. This concerns entities such as pension funds, charities, sovereign wealth funds and other organizations which may be exempt from tax, provided they meet all pertinent requirements under domestic tax law. Most States would grant treaty entitlement to such entities as the entities are seen as being liable to tax in the first step and relieved from that abstract liability to tax in the second step. Certain States such as the Netherlands, however, hold the opposite view, unless a particular DTC expressly provides otherwise. (Emphasis added.)[29]

Therefore, it should be noted that such a situation of double non-taxation arising from the application of complete distributive rules (as it is in the case at hand with the equivalent of article 13(4) of the OECD Model that allocates exclusive taxing rights to the residence state of the alienator) and domestic law is a direct consequence, maybe unfortunate to some extent, of the systematic structure of the Germany-Italy Income and Capital Tax Treaty (1989), which reproduces the OECD Model.

> [T]he ordinary meaning of the words has a legally imposed hermeneutical weight’ and that ‘recourse to methods that differ from textual interpretation is allowed only when the latter leads to obscure or conflicting conclusions.’ … A final argument of (international legal) relevance used by the *Corte* as further support to its findings consisted in referring to the Commentary on Articles of the OECD Model Tax Convention … In particular, the *Corte* acknowledged that, with respect to Article 17, the OECD Commentary expressly refers to the tax credit system as a means to offset double taxation (paras. 9 and 12), by that confirming the shared nature of the two States’ taxing rights.

See L. Marotti, Case note – *Corte di Cassazione* (Sez. tributaria civile), 24 Nov. 2016, No. 23984, *Patrizia Ciofi v. Agenzia delle entrate*, IYIL XXVI (2016), pp. 517 – 521.

23. *See* Scapa & Henie, *supra* n. 2.
24. E. Reimer et al., *Klaus Vogel on Double Taxation Conventions* p. 1077 (E. Reimer & A. Rust eds., 4th ed., Wolters Kluwer 2015).
25. *UN Model Double Taxation Convention between Developed and Developing Countries* (1 Jan. 2011), Models IBFD.
26. Reimer et al., *supra* n. 24, at p. 1077.
27. Paras. 29 and 30 *OECD Model: Commentary on Article 13* (2017).
28. Id., at para. 8.11.
29. Riemer et al., *supra* n. 24, at pp. 245 - 246.

5. Comparative Analysis: The *Lamesa Holdings* (1997) Case

From a comparative perspective, interestingly, the principles underlying CSC decision No. 25219 seem to be consistent with the results reached by some foreign courts, for example, the Australian Federal Court of Australia (FCA) in the famous *Lamesa Holdings* case,[30] which dealt with the sale of indirect interests in real property under the Australia-Netherlands Income Tax Treaty (1976).[31] In 1991, a US limited partnership, Leonard Green and Associates LP (LGA) decided to acquire an Australian mining company, Arimco Resources and Mining Company NL (Arimco), through interposed entities.[32] To this extent, a US limited partnership was created, Green Equity Investors LP (GEI) and, on 31 January 1992, GEI acquired the issued share capital of a company named Australian Resources Limited (ARL). On the same day, ARL then acquired the capital of a company named Australian Resources Mining Pty Limited (ARM). On 6 February 1992, GEI acquired the issued share capital of Lamesa, a private limited company incorporated in the Netherlands. GEI thereafter transferred the capital of ARL to Lamesa. On 23 February 1992, ARM successfully executed its takeover bid for Arimco. As a consequence, the whole capital of Arimco was owned by ARM.

A foreign holding company, Lamesa Holding BV (Lamesa), incorporated in the Netherlands, was used to enable the principals of GEI to benefit from the Australia-Netherlands Income Tax Treaty (1976). Lamesa (the taxpayer) sold the shares in ARL on 31 January 1994 and on 11 January 1996, realizing profits of USD 74,693,888 and USD 128,022,859 in, respectively, the 1994 and 1996 income tax year.

The issue in the case at hand concerned the proper interpretation of article 13(2)[33] of the Australia-Netherlands Income Tax Treaty (1976) and the interrelationship of that article with article 7. The issue was whether the alienation of real property article (article 13) applied to the profits derived by Lamesa, with Australia having the right to tax those profits.[34] If the article did not apply, the taxing right over those profits rested with the Netherlands but the Netherlands never asserted its right to tax the profits under its domestic tax law, i.e. the Dutch participation exemption. Consequently, if article 13 was held to be inapplicable, double non-taxation would arise.

The FCA noted that:

> The Agreement is an agreement for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income. Although, therefore, the Agreement has this dual object, *the Agreement substantially concerns allocation of taxing power* ... The allocation is of the right to tax. *There is nothing in the Agreement which compels a jurisdiction to exercise that right*. Australia, for example, does not tax "exempt income," although such income could fall within the business profits Article.
>
> *Save as to its operation to allocate taxing power, the Agreement is little concerned directly with fiscal evasion*. However, article 25 provides for an exchange of information between the competent authorities of each State, which exchange is vital to countering fiscal evasion. (Emphasis added.)

The FCA then stated that:

> If Art 13 applies, then profit from the alienation is authorized to be taxed in the place where the realty referred to in the Article is. If the alienation falls outside Art 13, then any profit falls to be taxed under Art 4, in this case in the Netherlands. *It happens to be the case, because of unilateral relief granted by the law of the Netherlands, that no tax will be payable in the Netherlands*. *That of itself can not affect the interpretation of the Agreement*. (Emphasis added.)

According to Lennard (2004), the courts in *Lamesa Holdings* recognized that double non-taxation may ultimately arise "simply" because one of the treaty parties chooses not to exercise its rights to tax under the tax treaty and it is accepted that countries need not exercise their full taxing rights under a tax treaty. In his opinion, the first instance judge in the *Lamesa Holdings* case was even clearer in rejecting the single tax principle.[35]

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30. AU: FCA, 20 Aug. 1997, *Lamesa Holdings BV v. Commissioner of Taxation*, NG 225 of 1997, Tax Treaty Case Law IBFD.
31. *Agreement between Australia and the Kingdom of the Netherlands for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income* (17 Mar. 1976), Treaties IBFD [hereinafter *Austrl.-Neth. Income Tax Treaty* (1976)].
32. Arimco, in turn, wholly owned Arimco Mining Pty Limited (Arimco Mining), which engaged in gold mining activities.
33. Art. 13 *Austrl.-Neth. Income Tax Treaty* (1976) reads as follows:
    1. Income from the alienation of real property may be taxed in the State in which that property is situated.
    2. For the purposes of this Article: (a) the term "real property" shall include: (i) a lease of land or any other *direct interest* in or over land; (ii) rights to exploit, or to explore for, natural resources; and (iii) shares or comparable interests in a company, the assets of which consist wholly or principally of *direct interests* in or over land in one of the States or of rights to exploit, or to explore for, natural resources in one of the States. (Emphasis added.)
34. The Commissioner argued that art. 13(2)(a) *Austrl.-Neth. Income and Capital Tax Treaty* (1976) applies to direct and indirect interests in real property. The Commissioner also contended that the court should look through the interposed entities and apply art. 13 to Lamesa's indirect interest in the gold mining leases. The difficulty for the Commissioner was that art. 13 expressly refers to direct interests in real property rather than just referring to interests in real property. The central theme was whether the FCA should have ignored the restriction of the interests in art. 13 to direct interests.
35. M. Lennard, *Australia*, in *Double non-taxation* Subject I [p. 150] (IFA Cahiers vol. 89a, IBFD 2004), Online Books IBFD states that: "The *Lamesa* first instance judge, whose decision had been unsuccessfully appealed from, had more explicitly rejected the proposition that the object and purpose of a DTA "*is not only to avoid double taxation*, *but also to ensure that tax is paid somewhere*" (emphasis added). Neither court, however, accepted that the necessary corollary of the object and purpose of preventing double taxation was that tax should be paid somewhere, to give effect (on one argument) to the object and purpose of preventing fiscal evasion; *see also* V. Crosland, *Australia: Double tax treaty protection-appeal lodged*, 8 Intl. Tax Rev. 7, p. 54 (July/Aug. 1997), who stated that: "An appeal has been lodged against the decision in Lamesa Holdings BV v FCT 97 ACT 4229. In that case, it was held that a Netherlands company (Lamesa) was not taxable in Australia on profits from the sale of shares in an Australian company, which was the holding company for a chain of Australian subsidiaries. The reasoning was that: '… the clear object and purpose of the Netherlands double tax treaty is that of avoiding double taxation, *not of ensuring that tax is paid in one of the contracting states. Therefore*, *although the result is that no tax will be paid anywhere*, *the clear words of Article 13 should not be departed from*.'" (Emphasis added.)

The Australian government was obviously unhappy with the results of the *Lamesa Holdings* case. Consequently, it amended the International Tax Agreements Act 1953 (the "Agreements Act")[36] to extend the scope of the alienation of real property article to situations in which interposed entities are used.[37] As mentioned, the taxpayer in the *Lamesa Holdings* case used two interposed entities to argue successfully that the alienation of real property article was inapplicable to profits from the sale of subsidiaries and that therefore the profits were not assessable in Australia. Taxation Laws Amendment Bill No. 11[38] was introduced on 9 December 1999 in the House of Representatives. Item 1 of Schedule 1 proposed the inclusion of section 3A in the Agreements Act. The operative provision was sub-section 3A(2), which states that:

> alienation of income provisions in Australia's treaties are extended to indirect interests in real property held through interposed entities. If the value of the interposed entities is principally attributable to real property, this subsection allows the alienation of real property article to apply to any interests in interposed entities.

6. Solutions Proposed

So, what can contracting states do in order to avoid these situations of double non-taxation? The majority of scholars believe that contracting states may implement a measure in a tax treaty, for example, a subject-to-tax clause, giving the source state (Italy) the right to exercise its taxing rights in cases where the residence state (Germany) does not tax the income (capital gain) under its domestic law (section 8b(2) of the KStG).[39] So, as suggested by Lang, Italy may require an amendment of the Germany-Italy Income and Capital Tax Treaty (1989) and negotiate the insertion of a subject-to-tax clause similar to that included in article 15 of the Protocol to the France-Italy Income and Capital Tax Treaty (1989), according to which:

> In the cases where, in accordance with the provisions of this Convention, income must be exempted by one of the States, the exemption shall be granted if and to the extent such income is taxable in the other State.[40]

Thus, the France-Italy Income and Capital Tax Treaty (1989) links exemption in Italy to taxation in France. Conci and Mayr (2004)[41] argued that historically Italy was not interested in negotiating "subject-to-tax" clauses because it has adopted the credit method. Therefore, these clauses are inserted into tax treaties at the request of the other contracting states that adopt the exemption method. In this regard, it is highly likely that article 15 of the Protocol to the France-Italy Income and Capital Tax Treaty (1989) was negotiated by and inserted into the tax treaty at the request of France since it had made a reservation to the Commentary on Article 13(5) of the OECD Model. Accordingly, France can accept the provisions of article 13(5) of the OECD Model, but wishes to retain the possibility of applying the provisions in its laws relative to the taxation of gains from the alienation of shares or rights which are part of a substantial participation in a company which is a resident of France. Nonetheless, it is very unclear, from a tax policy perspective, why the Italian treaty negotiators did not include such provision in the Germany-Italy Income and Capital Tax Treaty (1989). Indeed, both tax treaties were concluded around mid-October 1989. In particular, the Germany-Italy Income and Capital Tax Treaty (1989) was concluded two weeks after the France-Italy Income and Capital Tax Treaty (1989), which was signed in Venice on 5 October 1989. In the authors' opinion, if a similar provision to article 15 of the Protocol to the France-Italy Income and Capital Tax Treaty (1989) had been included in the Germany-Italy Income and Capital Tax Treaty (1989) as well, the CSC would have reached a different result in the case at hand, since Italy as source state could have taxed the capital gains if the other state – i.e. the residence state, Germany – did not exercise its right to tax pursuant to domestic law.

Such view is also confirmed by case law concerning situations of double non-taxation arising for Italian resident taxpayers earning their employment income abroad. Up to 31 December 2000, employment income earned abroad was exempt from tax on the basis of Italian domestic law.[42] Therefore, in those cases, double non-taxation of employment income occurred when the foreign source state – France

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36. AU: International Tax Agreements Act 1953.
37. *See* R. Snoeij, *The Amendment of Australia's Domestic Law after the Lamesa Case: A Lesson to be Learned from Dutch Case Law?* , 35 Intertax 10, pp. 548-554 (2007).
38. AU: Taxation Laws Amendment Bill No. 11.
39. *See also* Scapa & Henie, *supra* n. 2 ; *see also* E. Reimer et al., *supra* n. 24 , at p. 1077, who states that: "If, however, the treaty contains a general subject-to-tax-clause and the capital gain is not taxed in the residence State, taxation in the source State is maintained"; P. Arginelli & G. Cuzzolaro, *Sull'applicabilità delle Convenzioni contro le doppie imposizioni in assenza di un'effettiva duplicazione d'imposta* , Rivista di Diritto Tributario, supplemento online (6 Dec. 2018), available at http://www.rivistadirittotributario.it/2018/12/06/sullapplicabilita-delle-convenzioni-le-doppie-imposizioni-assenza-uneffettiva-duplicazione-dimposta/ (accessed 8 Jan. 2019); and M. Lang, *General Report* , in *Double non-taxation* Subject I [pp. 85 – 86] (IFA Cahiers vol. 89a, IBFD 2004), Online Books IBFD pp. 85-86, who notes that: "it must be assumed that the contracting states accepted that the national tax systems are subject to change and that a contracting state may at a later stage decide not to exercise a right to tax assigned to it by the convention. This may trigger double non-taxation if the other contracting state is still prevented from taxation pursuant to the treaty provisions. This consequence is not in contradiction with the objective and purpose of the DTC provision. If the contracting states want to ensure that the convention does not lead to cases of double non-taxation in the future, this cannot be achieved by way of interpretation. Instead, this will require an amendment of the convention … Moreover, various forms of 'subject-to-tax' clauses also aim at achieving this objective [that single taxation is applied]. In recent years, states have increasingly agreed on rules within the scope of application of the exemption method, according to which exemption in one state depends on whether the other contracting state exercises the taxation right assigned to it by the convention. *These rules* … clearly *serve to ensure single taxation* ." (Emphasis added.)
40. *See also* *Convention between the Government of the Republic of Italy and the Government of the Republic of Zambia for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect To Taxes on Income* art. 18 (27 Oct. 1972) (as amended through 1980), Treaties IBFD, which reads: "Subject to the provisions of paragraph 1 of Article 19, any pension or similar remuneration derived from sources within a Contracting State in consideration of past employment by an individual who is a resident of the other Contracting State and *subject to tax* in respect thereof in that other Contracting State, *shall be exempt from tax* in the first-mentioned Contracting State" (emphasis added).
41. P. Conci & S. Mayr, *Italy* , in *Double non-taxation* Subject I [at p. 464] (IFA Cahiers vol. 89a, IBFD 2004), Online Books IBFD.
42. Under IT: *Decreto del Presidente della Repubblica* (Presidential Decree) No. 917 of 1986, art. 3(3)(c), income from employment exercised abroad on a regular basis and under an exclusive relationship was excluded from the basis of taxation. IT: *Decreto Legislativo* (Legislative Decree) No. 314 of 2 September 1997, para. 5(1)(a) abolished art. 3(3)(c) with effect from 1 Jan. 2001.

– did not tax this income in accordance with a treaty provision, i.e. article 15(4) of the France–Italy Income and Capital Tax Treaty (1989), which attributed to Italy an exclusive right to tax.[43]The Provincial Tax Commission of Sanremo in Decision No. 256 of 22 March 1996[44]and the Provincial Tax Commission of Imperia in Decision No. 381 of 26 June 1997[45]held that article 15 of the Protocol to the France-Italy Income and Capital Tax Treaty (1989) expressly provides that the non-taxation in France, in other words, the waiver by France of its power to tax, is granted if, and to the extent, that such income is in any case taxable in Italy. Substantially, Italy and France agreed by article 15 of the Protocol that, in those cases where an item of income must be exempt in one of the two states (France in the case at hand pursuant to article 15(4) of the tax treaty), exemption is granted (in France) if and to the extent such income is in any case taxable in Italy. However, due to the fact that such income is not taxed in Italy as a consequence of domestic tax law (art. 3(3)(c) of *Decreto del Presidente della Repubblica* (Presidential Decree) No. 917 of 1986), the right to tax such employment income reverts back to France[46]thanks to article 15 of the Protocol and by way of derogation from article 15(4) of the France-Italy Income and Capital Tax Treaty (1989). In such a way, there is no double exemption and double exemption should in any way be pursued by France as source state where the employment income was generated.

Finally, Conci and Mayr (2004) seem to share this view.[47]However, it should be noted that they refer to the hypothetical case of Italy as residence state. Thus, their example refers to the case where capital gains are realized by Italian companies on the disposal of foreign shareholdings. In their opinion, if the tax treaty contains a subject-to-tax clause, the source state may tax the capital gains if they are not taxed in Italy. Since article 15 of the Protocol to the France-Italy Income and Capital Tax Treaty (1989) is a reciprocal provision, the authors believe that it can also be applied the other way around, i.e. where Italy as source state may tax the capital gains if they are not taxed in France.[48]Thus, in a hypothetical situation where French companies realized a capital gain from the disposal of Italian shareholdings and the capital gain is exempt in France, the right to tax should revert back to Italy.

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43. Art. 15(4) *Fr.-Italy Income and Capital Tax Treaty* (1989) reads: "Notwithstanding the preceding provisions of this Article, employment income of persons living in the frontier zone of one of the States and working in the frontier zone of the other State *shall be taxable only* in the State of which such a person is resident" (emphasis added). The cases at hand concerned the treatment of employment income earned by frontier workers. The taxpayers were resident in Liguria, one of three Italian regions neighbouring France. According to art. 9 of the Protocol to the *Fr.-Italy Income and Capital Tax Treaty* (1989), frontier zones should be understood to mean those areas in Italy and those departments in France which are adjacent to the border.
44. IT: CTPL, 22 Mar. 1996, Decision No. 256, Tax Treaty Case Law IBFD.
45. IT: CPTI, 26 June 1997, Decision No. 381, Tax Treaty Case Law IBFD.
46. Id., at C. Innamorato, Summary, where it is stated that: "The Tax Court … held that Art. 15(4) attributed to Italy in the case at hand an exclusive right to tax. However, since Italy could not tax this income under its domestic law … and the treaty could not be read as creating such a right to tax, Italy could not tax the taxpayer's French employment income. The Court then referred to Point 15 of the Protocol to the treaty on the basis of which France is obliged to give up its right to tax the employment income under Art. 15(4) of the treaty only if that income is taxed in Italy. Consequently, since in the case at hand Italy did not impose any tax, the employment income of the Italian frontier worker was taxable in France."
47. *See* Conci & Mayr, *supra* n. 41 , at p. 470, who state that: "It is very rare for taxpayers resident in Italy to benefit from a double exemption because Italy adopts the credit method in its treaties. Double non-taxation may arise from the Tax Reform of 2004 which grants to Italian companies exemption from tax on capital gains derived from the disposal of foreign shareholdings registered as financial assets. If the state of source is not allowed to tax this capital gain, double non-taxation occurs. This double non-taxation (accepted under the OECD model) is, however, eliminated in the Italy-France treaty (1989) by means of 'subject-to-tax' clause (no. 15 of the protocol) whereby France as state of source may tax the capital gains if they are not taxed in Italy." *See also* Conci & Mayr, *supra* n. 41 , at p. 476, where these authors state that: "We can mention the following clauses: in the Italy-France treaty (1989), no. 15 of the protocol stipulates that the exemption in one contracting state provided under the treaty only applies if the income is taxed in the other contracting state. If, therefore, France cannot tax, in accordance with article 13 paragraph 5 of the treaty, the capital gain derived from the disposal of a non-qualified shareholding, the right to tax reverts back France, if the seller of the shareholding is an Italian company and the capital gain is exempt in Italy."
48. In addition, Conci & Mayr *supra* n. 41 , at p. 470 noted that two tax treaties, *Convention between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Italian Republic for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income* (21 Oct. 1988), Treaties IBFD [hereinafter *Italy-U.K. Income Tax Treaty* (1988)] and *Convention between the Government of the Italian Republic and the Government of the Republic of South Africa for the Avoidance of Double Taxation with Respect to Taxes on Income and for the Prevention of Fiscal Evasion* (16 Nov. 1995), Treaties IBFD [hereinafter *Italy-S. Afr. Income Tax Treaty* (1995)] contain a clause whereby non-taxation in the state of residence is a reason for taxation in the state of source.
    Art. 13(5) *Italy-U.K. Income Tax Treaty* (1988) reads as follows:
    > The provisions of paragraph 4 of this Article shall not affect the right of a Contracting State to levy according to its law a tax on gains from the alienation of any property derived by an individual who:
    > (a) is a resident of the other Contracting State; and
    > (b) has been a resident of the first-mentioned Contracting State at any time during the five years immediately preceding the alienation of the property; and
    > (c) *is not subject to tax on those gains in the other Contracting State* . (Emphasis added.)

    See also article 13(5) of the *Italy-S. Afr. Income Tax Treaty* (1995), which reads:
    > The provisions of paragraph 4 of this Article shall not affect the right of a Contracting State to levy according to its law a tax on gains from the alienation of any property derived by an individual who:
    > (a) is a resident of the other Contracting State; and
    > (b) has been a resident of the first-mentioned Contracting State at any time during the years immediately preceding the alienation of the property; and
    > (c) such property was acquired while the individual was a resident of the first-mentioned State; and
    > (d) *is not subject to tax on those gains in the other Contracting State* . (Emphasis added.)

    If the Italian government wishes to renegotiate the *Ger.-Italy Income and Capital Tax Treaty* (1989) in order to avoid results of Decision No. 25219 (2018), *supra* n. 1 , it may negotiate a similar clause to those included in the *Italy-U.K. Income Tax Treaty* (1988) and the *Italy-S. Afr. Income Tax Treaty* (1995), obviously without including requirements provided by art. 13(5)(b) and (c) *Italy-S. Afr. Income Tax Treaty* (1995).

7. Can a Line Be Drawn between Proper and Improper Double Non-taxation?

The results reached by the CSC in Decision No. 25219 appear to contrast starkly with the previous Decision No. 23367 given on 6 October 2017.[49] On the one hand, the CSC in Decision No. 25219 seems to allow double non-taxation, considering it to be a legitimate result from the application of the tax treaty, while, on the other, the CSC in Decision No. 23367 seems to consider it an illegitimate and improper result. This latter case concerned the tax treatment of EU cross-border corporate dividends. Dividends were paid by an Italian subsidiary to its French parent company in 2003. Italy thus was the "source state" and the case concerned the tax treatment of outbound dividends.

In 2003, the Italian system of taxation of corporate profits was based on the imputation model. As noted by Garbarino (2013),[50] in 1990, before the implementation of the Parent-Subsidiary Directive (90/435) in 1992,[51] domestic dividends were fully taxable, but a tax credit equal to 100% of the underlying corporate income tax paid by the distributing company, in respect of the profits distributed, was granted to Italian companies. Inbound dividends were 60% exempt from corporate tax if the Italian company held, in the case of a foreign unlisted distributing company as well as in the case of a foreign listed distributing company, at least 20% of its capital in terms of voting rights. Inbound dividends were fully taxable if those requirements were not satisfied. In 2000, the imputation system was extended to dividends distributed from non-black list countries. A few tax treaties, like the France-Italy Income and Capital Tax Treaty (1989)[52] or the Italy-United Kingdom Income and Capital Tax Treaty (1988),[53] granted a partial tax credit or a refund for foreign taxes paid by the distributing foreign company.

Under article 10(4)(b) of the France-Italy Income and Capital Tax Treaty (1989):

> 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.

According to articles 145 and 216 of the French *Code Général des Impôts* (General Tax Code, CGI)[54] implementing the provisions of the Parent-Subsidiary Directive (90/435),[55] French resident parent companies may opt for the participation exemption regime with respect to dividends received from foreign subsidiaries.[56]

Thus, based on article 10(4)(b) of the France-Italy Income and Capital Tax Treaty (1989), the French parent company filed a claim with the Italian Revenue Agency asking for a tax credit refund, which was rejected. The French parent company appealed the denial but lost before both the Provincial Tax Commission and the Regional Tax Commission. The case was ultimately remitted to the CSC.[57] The French parent company argued that the denial violated article 10(4)(b) of the France-Italy Income and Capital Tax Treaty (1989). In its opinion, the fact that the inbound dividends were excluded from its taxable income should not prevent the application of article 10(4)(b), since article 10 of the France-Italy Income and Capital Tax Treaty (1989) requires that the parent company is subject to tax without it

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49. IT: CSC, 6 Oct. 2017, Decision No. 23367. ***See also*** IT: CTPP, 4 Nov. 2011, Decision No. 148, Tax Treaty Case Law IBFD. ***See again*** P.F. Tripoli, *Turin Tax Court Denies Treaty Residence State Dividend Exemption Absent Source Taxation: No Country for Economic Double Taxation Relief?*, 51 Eur. Taxn. 6 (2011), Journals IBFD. However, here Italy was the "residence state" and the case concerned the tax treatment of inbound dividends. According to art. 24(2)(b) *Ger.-Italy Income and Capital Tax Treaty* (1989), "Income from dividends referred to in subparagraph (a) of paragraph 6 of Article 10 ***shall be excluded*** from the base upon which Italian tax is levied if the dividends are paid to a company (not including partnerships) being a resident of the Italian Republic by a company being a resident of the Federal Republic of Germany at least 25% of the capital of which is owned directly by the Italian company" (emphasis added). In 2004, the Italian Revenue Agency denied an Italian shareholder a full exclusion from corporate income tax on dividends received from a Germany subsidiary in 2004, as, in its opinion, 5% of the dividends were taxable at the ordinary corporate tax rate of 33% under the Italian participation exemption, which provides for a 95%. According to the Italian Revenue Agency, the simultaneous application of Council Directive 2011/96/EU of 30 November 2011 on the Common System of Taxation Applicable in the Case of Parent Companies and Subsidiaries of Different Member States, OJ C 107 (2011), EU Law IBFD [hereinafter Parent-Subsidiary Directive (2011/96)] (no withholding tax was levied at source) and art. 24(2)(b) *Ger.-Italy Income and Capital Tax Treaty* (1989) can lead to juridical double non-taxation of such dividends. Assuming that the simultaneous application of the Parent-Subsidiary Directive (2011/96) and the *Ger.-Italy Income and Capital Tax Treaty* (1989) is lawful as argued by some practitioners, the authors are not quite sure whether this can be advantageous for the Italian company receiving dividends since a full exemption does not allow the deduction of expenses as there is no taxable portion of received dividends that can absorb costs that are related to the flow of dividends. On the other hand, it should be noted that art. 24(2)(b) *Ger.-Italy Income and Capital Tax Treaty* (1989) actually uses the word "excluded" rather than "exempt" meaning that the item of income is not taxable but related costs can be deducted.
50. C. Garbarino, *Taxation of EU Cross-Border Corporate Dividends: Convergence and Tax Competition*, Bocconi Leg. Stud. Research Paper No. 2298085, p. 5 (25 July 2013), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2298085 (accessed 29 Jan. 2019).
51. Council Directive of 23 July 1990 on the Common System of Taxation Applicable in the Case of Parent Companies and Subsidiaries of Different Member States (90/435/EEC), OJ L 225 (1990), EU Law IBFD [hereinafter Parent-Subsidiary Directive (90/435)].
52. Art. 10(4)(b) *Fr.-Italy Income and Capital Tax Treaty* (1989).
53. Art. 10(3) and (4) *Italy-U.K. Income Tax Treaty* (1988).
54. FR: *Code Général des Impôts* (General Tax Code, CGI).
55. According to art. 4 Parent-Subsidiary Directive (90/435), where a parent company, by virtue of its association with its subsidiary, receives distributed profits, the state of the parent company should either refrain from taxing such profits, or tax such profits while authorizing the parent company to deduct from the amount of tax due that fraction of the corporation tax paid by the subsidiary which relates to those profits. Again, according to art. 5 Parent-Subsidiary Directive (90/435), profits which a subsidiary distributed to its parent company should, at least where the latter holds a minimum of 25% of the capital of the subsidiary, be exempt from withholding tax.
56. In such a case, dividends are exempt. A lump sum of 5% of the gross dividends, deemed to represent non-deductible expenses, is added back to taxable income and taxed at the standard rate of corporate income tax (with effect from 1 Jan. 2016, the rate of the add-back is 1% for dividends received from certain companies located in European Economic Area (EEA) countries). In order to qualify as a parent company, the French company must have a shareholding of 5% or more of the capital of the foreign company at the date of the distribution and hold the shares for at least 2 years. *See* P. Burg, *France – Corporate Taxation* sec. 7., Country Analyses IBFD (accessed 10 Jan. 2019).
57. IT: CSC, Decision No. 23367 (6 Oct. 2017).

being necessary that dividends have been effectively taxed in the hands of the recipient in its residence state. According to the plaintiff, an effective taxation is only required when the recipient company has a non-qualified participation in the dividends distributing company. The CSC rejected the plaintiff's claim in light of the following two reasons:

(1) Article 7(2) of the Parent-Subsidiary Directive (90/435) does not mean that the benefits deriving from Community legislation may be cumulated with those deriving from the rules of the France-Italy Income and Capital Tax Treaty (1989).[58] These must be considered as alternatives, since the sum of the exemption and the tax credit would go beyond the aim of avoiding double taxation, leading to a so-called situation of double non-taxation.

(2) Double non-taxation would result in a sort of tax concession, a so-called notional tax credit. In this regard, the CSC noted that, in an effort to foster economic development, bilateral tax treaties with developing and/or emerging countries usually contain a tax sparing provision. On the other hand, article 15 of the Protocol to the France-Italy Income and Capital Tax Treaty (1989) avoids situations of double exemption, being a typical subject-to-tax clause. If a French recipient of inbound exempt dividends obtains the *avoir fiscal* as well, it would get two tax benefits, and the fact that a 5% withholding tax is applied on one of them (the tax credit) reduces to some extent the distortion created by double non-taxation, but does not entirely eliminate it.

With regard to the meaning of the wording "subject to tax", the CSC held that plaintiff's claim is in contrast with previous case law on tax treatment of cross-border dividends, which requires that the term has to be understood as application of actual taxation, i.e. as effectively taxed. In order to support its arguments, the CSC also referred to the case law of the Court of Justice of the European Union (ECJ), in particular to *Océ van der Grinten* (Case C-58/01), according to which:

> The tax credit is a fiscal instrument designed to avoid double taxation, in economic terms, first in the hands of the subsidiary and then in the hands of the parent company in receipt of the dividends, of the profits distributed as dividends;[59]

And *Wereldhave Belgium and Others* (Case C-448/15), where it is stated that:

> Where a parent company... is entitled under the legislation of its Member State of establishment to a zero rate of taxation for all its profits, provided that all those profits are distributed to its shareholders, the risk of double taxation on the part of that parent company of profits which were distributed to it by its subsidiary is ruled out.[60]

In this case, since inbound dividends are exempt in France, the tax credit would go beyond the aim of avoiding double taxation intended, according to the classical distinction, as juridical double taxation (taxation of the same income twice in the hands of the same person) and economic double taxation (taxation of the same income in the hands of different persons, i.e. the simultaneous taxation of a company's profits at the level of the company and of the dividends at the level of the shareholders).

The CSC concluded by holding that a French parent company receiving dividends from its Italian subsidiary that were exempt from taxation in France as a result of the implementation of the Parent-Subsidiary Directive (90/435) is not entitled to the tax credit provided by article 10(4)(b) of the France-Italy Income and Capital Tax Treaty (1989) because the exemption under the Directive excludes that double taxation which the treaty credit aims at neutralizing. Simply stated, taxation in the residence state (France) is required for the payment of dividend tax credits in the state of source (Italy).[61]

In the authors' opinion, since double economic taxation had already been addressed by the French participation exemption, there was no need for the French parent company to ask for a refund for tax credits, thereby eliminating partially the corporate income tax paid by the Italian subsidiary. Article 10(4)(b) of the France-Italy Income and Capital Tax Treaty (1989) had a reason to exist when both countries were under the imputation system. Since both countries migrated to the exemption system in 2004,[62] article 10(4)(b) of the France-Italy Income and Capital Tax Treaty (1989) might be considered to have been implicitly abrogated. Thus, even though the underlying principle of the decision might be shared, i.e. the Parent-Subsidiary Directive (90/435) and treaty provisions cannot be applied jointly because, otherwise, they would give rise to double non-taxation. What the authors find problematic and consider to be a question left unanswered by those who commented the decision is the means: Can a domestic court unilaterally nullify the application of international treaty obligations? In other words, can domestic courts override a treaty provision if its literal application coupled with domestic tax law would result in double non-taxation? In the authors' opinion, the denunciation of the tax treaty would be a better option. Accordingly, the Italian competent tax authorities should communicate to their French peers that article 10(4)(b) of the France-Italy Income and Capital Tax Treaty (1989) is no longer available following the migration of both states to the exemption system in 2004.

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58. Art. 7(2) Parent-Subsidiary Directive (90/435) reads as follows: "This 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".
59. UK: ECJ, 25 Sept. 2003, Case C-58/01 , *Océ Van der Grinten NV v. Commissioners of Inland Revenue* , para. 56, ECJ Case Law IBFD.
60. BE: ECJ, 8 Mar. 2017, Case C-448/15 , *Belgische Staat v. Wereldhave Belgium Comm. VA and Others* , para. 40, ECJ Case Law IBFD.
61. *See* Conci & Mayr, *supra* n. 41 , at p. 477, where it is stated that: "Under certain conditions, Italy grants to shareholders resident in France and in the UK a partial tax credit on dividends (the payment of the dividend tax credit within the framework of the imputation system will, however, be abolished by the Tax Reform of 2004). In certain cases, the dividends are required to be subject to tax in the other contracting state."
62. P. Gariboldi & M. Starita, *Participation Exemption in the Italian Tax Reform* , 32 Intertax 12, pp. 607-613 (2004) and F. Nobili & M.A. Lanza, *Synthesis of Italian Tax Reform* , 32 Intertax 11, pp. 564-566 (2004).

8. Conclusions

Since 1997, the first author has argued that the core of the international tax regime has two norms, which he calls the benefits principle (active business income should be taxed primarily at source, while passive investment income should be taxed primarily at residence) and the single tax principle (income should be taxed once, i.e. not more and but also not less than once).[63] What this means in practice is that, if the jurisdiction that has the primary right to tax refrains from doing so, the other jurisdiction should tax to prevent double non-taxation. This thesis is quite controversial. While most commentators would agree that the benefits principle is clearly embodied in the text of the over 3,000 tax treaties, several prominent international tax academics and practitioners in the United States and elsewhere deny the validity of the single tax principle and some doubt its coherence.[64]

Archival research conducted at the Historical & Special Collections of Harvard Law School Library shows that the origins of the single tax principle, in other words, the rejection of double non-taxation, under tax treaties, can be traced to the eight-year period from 1961 to 1969 when Stanley Surrey, a Harvard law professor (1950-1984) became the first US Assistant Secretary of the Treasury for Tax Policy. As far as tax treaties are concerned, Surrey made three major contributions to applying the single tax principle in practice. First, the tax treaties negotiated by Surrey (for example, the Luxembourg-United States Income and Capital Tax Treaty (1962),[65] the Netherlands Antilles-United States Income Tax Treaty (1948)[66] and the Canada-United States Income Tax Treaty (1966))[67] took pains to enforce source-based taxation in cases where there was no residence-based taxation of passive income. The Luxembourg-United States Income and Capital Tax Treaty (1962) was the first US tax treaty indicating that the double non-taxation of US-source income was no longer to be tolerated. Article XV of the Luxembourg-United States Income and Capital Tax Treaty (1962) denied treaty benefits to, "any holding company entitled to any special tax benefit under Luxembourg Law of July 31, 1929, and Decree Law of December 27, 1937, or under any similar law subsequently enacted...". At that time, Luxembourg laws exempted holding companies from all direct taxes otherwise imposed by Luxembourg, and dividends and interest paid by such holding companies were not subject to the withholding tax at source. The official explanation proposed by the US Treasury Department on article XV of the Luxembourg-United States Income and Capital Tax Treaty (1962) interestingly stated that:

> *Inasmuch as these laws allow investment income from domestic and foreign sources to be accumulated by these holding companies and distributed to nonresident individuals and foreign corporations without the imposition of Luxembourg tax, it was deemed appropriate not to grant any of the exemptions from, or reductions in the rate of, U.S. tax otherwise available under this convention with respect to such income* ... Although this approach adopted for the purpose of excluding so-called "tax haven" income from the scope of the convention is not found in any income tax convention concluded by the United States, other than the Netherlands Antilles Protocol, certain precedent may be found in some of the relief provisions contained in the conventions with the United Kingdom, Ireland, Australia, and Pakistan requiring that the recipient of treaty income be "subject to tax" on such income in the country of residence in order to qualify for exemption from, or reduction in the rate of, the tax of the country of source. *Moreover, this new provision is consistent with the spirit of the provisions of section 12 of the Revenue Act of 1962 relating to the taxation of certain "tax-haven" income of controlled foreign corporations to U.S. shareholders.* (Emphasis added.)

Similar language appeared in article I of the Protocol (1963) to the Netherlands Antilles-United States Income Tax Treaty (1948), according to which:

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63. *See* , for example, R.S. Avi-Yonah, *Commentary on Rosenbloom* , 53 Tax L. Rev. 167 (2000); Y. Brauner, *An International Tax Regime in Crystallization* , 56 Tax L. Rev. 259; F.B. Brown, *An Equity-Based, Multilateral Approach for Sourcing Income Among Nations* , 11 Fla. Tax Rev. 565; E. Farah, *Mandatory Arbitration of International Tax Disputes: A Solution in Search of a Problem* , 9 Fla. Tax Rev. 703; V. Thuronyi, *International Tax Cooperation and a Multilateral Treaty* , 26 Brooklyn J. Int'l L. 1641.
64. *See* , for example, H.D. Rosenbloom, *International Tax Arbitrage and the "International Tax System"* , 53 Tax L. Rev. 137 (2000); M.J. Graetz, *Taxing International Income - Inadequate Principles, Outdated Concepts, and Unsatisfactory Policy* , 54 Tax Law Review 261 (2001); J. Roin, *Taxation Without Coordination* (2002), available at http://papers.ssrn.com/paper.taf?abstract_id=302141; M.A. Kane, *Strategy and Cooperation in National Responses to International Tax Arbitage* , 53 Emory L.J. 89; A.H. Rosenzweig, *Harnessing the Costs of International Tax Arbitrage* , 26 Va. Tax Rev. 555.
65. *Convention between the United States of America and the Grand Duchy of Luxembourg with Respect to Taxes on Income and Property* (18 Dec. 1962), Treaties IBFD.
66. *Convention between the United States of America and the Netherlands Antilles with Respect to Taxes on Income* (29 Apr. 1948) (as amended through 1963), Treaties IBFD.
67. *Convention between the United States of America and Canada Relating to the Avoidance of Double Taxation and Prevention of Fiscal Evasion in the Case of Income Taxes* (4 Mar. 1942) (as amended through 1966), Treaties IBFD [hereinafter *Can.-U.S. Income Tax Treaty* (1942)]. *Supplementary Convention between Canada and the United States of America further Modifying and Supplementing the Convention and Accompanying Protocol of March 4, 1942 for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion in the Case of Income Taxes as Modified by the Supplementary Convention of June 12, 1950 and the Supplementary Convention of August 8, 1956* (25 Oct. 1966), Treaties IBFD added the following new para. to art. XI:

    6. Paragraph 1 of this Article shall not apply in respect of income derived from sources in one of the Contracting States and paid to a corporation organized under the laws of the other Contracting State if such corporation *is not subject to tax* by the last-mentioned Contracting State on that income because it is not a resident of the last-mentioned Contracting State for purposes of its income tax.

    The US government wanted to close the loophole made possible by the interaction of Canadian tax law and the *Can.-U.S. Income Tax Treaty* (1942). This had produced a situation in which US taxes could be avoided by persons living outside both countries. The *Can.-U.S. Income Tax Treaty* (1942) provided that a company organized in Canada, which received investment income from the United States, was subject to the 15% US withholding tax instead of the customary 30%. Canadian law further provided that a domestic corporation controlled and managed outside Canada deriving income from outside the country was exempt from Canadian taxes. Persons residing in a country which had no tax treaty with the United States could thus use a Canadian-organized holding or investment company, which was controlled and managed in a "tax haven" country to make investments in the United States at a tax cost of only 15% with no tax at all in Canada or in their home country. This situation was similar to the eliminated loophole involving the Netherlands Antilles. It should be noted that the 1966 budget submitted to the Canadian Parliament by Finance Minister Walter Gordon contained a provision for taxing corporations, which were incorporated in Canada and then moved their headquarters outside the country. *See Loophole under Canadian tax treaty to be "plugged"* , J. Taxn., p. 362 (June 1965).

Articles VII, VIII, and IX of the Convention shall not apply to income derived from sources within the United States by any investment or holding company, corporation, limited partnership or other entity entitled to any of the special tax benefits provided under Article 13, Article 14, or Article 14A of the Netherlands Antilles' National Ordinance on Profit Tax of 1940, as in effect on September 1, 1963, or to substantially similar tax benefits granted under any law of the Netherlands Antilles enacted after such date.[68]

Again, the official explanation of the US Treasury Department stated the reasons behind article I of the 1963 protocol. The combination of reduced treaty withholding tax rates and special Antillean tax rates for investment companies and holding companies resulted in a maximum effective tax burden on investment income derived by an Antillean corporation from US sources of 17.55% in the case of dividends and only 3% in the case of interest and royalties. In addition, non-resident shareholders in Antillean corporations were not subject to Antillean taxation on dividends from those corporations. This favourable tax atmosphere for investment in the United States through an Antillean corporation increased the number of non-resident-owned investment and holding companies to 986 by January 1963 according to data provided by the Netherlands Antilles government to the Treasury Department. In this regard, the US Treasury Department stated that:

... when residents of third countries are lured into holding their U.S. investments in a company incorporated in a treaty country through artificial reduction by that country of its own tax rates on the income, the primary purpose of a tax treaty is subverted. Tax treaties are governmental agreements designed to prevent double (and therefore excessive) *taxation* of an investor's foreign source income by resolving conflicting jurisdictional claims to tax which arise because one country is the source of the income and the other is the residence of the recipient. *Exemptions and reductions in source taxation provided for by treaty are reciprocal revenue adjustments between governments* designed to implement a tax credit for foreign taxes paid. *They are not intended to reduce the tax burden of the investor, as it is assumed that the tax waived by the source country will be imposed by the destination country. Exemptions and reductions in U.S. tax on United States source income paid to nonresident-owned Antillean investment and holding companies are not justified as long as this income is taxed at low rates (not exceeding 3 per cent at present) in the Netherlands Antilles. It is therefore deemed necessary to restore the U.S. statutory rate of tax on dividends, interest, and royalties derived from U.S. sources by Antillean investment and holding companies.* Article I of the protocol accomplishes this without denying treaty tax benefits to Antillean residents or to those Antillean corporations which are wholly owned by Antillean residents or by residents or corporations of the Netherlands. (Emphasis added.)[69]

So, what is the theoretical justification of provisions of this kind? If preferential measures, special tax benefits, etc. substantially mitigate taxation by the residence state, then there is little danger of double taxation, and cession by a source state of its right to tax is inappropriate. For those reasons, the authors believe that Surrey invented the single tax principle from the perspective of the United States as a source state. Thus, it could be argued that, in 1962, Surrey reversed the course of US tax policy in regard to US-source income earned by non-residents by placing significant limits on double non-taxation.

Second, the Foreign Investors Tax Act of 1966[70] changed considerably the system of taxation for non-resident aliens and foreign corporations. The 1966 changes to inbound investment ensured the separation of passive income of foreign investors from their active income, thereby making it more likely that each would be taxed appropriately (and that active income would be taxed more at source, in accordance with the benefits principle). According to Roberts and Warren (1967), one of the principal objectives of the Foreign Investors Tax Act was to prevent the United States from being used as a "tax haven", in the sense that this means the substantial avoidance of tax in the home country and as well as the source state.[71] The Ways and Means Report illustrated the use of the United States as a tax haven by the following situation.[72] A foreign corporation was organized under the laws of a country which did not tax such corporations on income derived from the conduct of a business outside the country. It organized a sales office in the United States to sell its products in countries other than the United States and the country of incorporation. The foreign corporation avoided tax by the home country because the business was not conducted there. It avoided taxation by the United States because, under the title-passage rule, the income was not derived from US sources and it could avoid tax by the countries in which the product was sold because it had no PE there. Finally, the Ways and Means Report stated that similar tax avoidance schemes existed in the case of rents and royalties from a licensing business, and income from banking, financing, or investment company business.

Third, it was during Surrey's time at the US Treasury Department that the US Delegation wrote two notes to the OECD Fiscal Committee recommending the establishment of a new Working Group which would address the problem of Tax Avoidance through the improper use or Abuse of tax Conventions. In a note written on 14 November 1961, it was stated that:

In recent years there has developed a problem of tax avoidance and evasion to which it would be appropriate for the Fiscal Committee to address itself. *This problem involves the exploitation of tax conventions in a manner which is unnecessary for the avoidance of double taxation and which provides unintended benefits to taxpayers*. For example, an enterprise of one contracting country may establish a corporate subsidiary in the other contracting country principally for the purpose of taking advantage of the interaction of

68. Protocol Modifying and Supplementing the Extension to the Netherlands Antilles of the Convention between the United States of America and the Kingdom of the Netherlands for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Certain Other Taxes (23 Oct. 1963) [hereinafter Protocol Neth.-USA Income Tax Treaty (1963)].
69. Statement of Treasury Department with respect to the *Protocol Neth.-USA Income Tax Treaty* (1963).
70. US: Foreign Investors Tax Act of 1966.
71. S.I. Roberts & W.C. Warren, *The Foreign Investors Tax Act: what it covers, whom it affects, how it works*, J. Taxn., p. 47 (Jan. 1967). In the opinion of these authors, the major impact of this objective appeared in provisions which, for the first time, taxed income from foreign sources where that such income was effectively connected with an office or other fixed place of business in the United States.
72. Id., at p. 47. *See also* US: Hearings on H.R. 5916 before the House Committee on Ways and Means, 89th Cong., 1st Sess. (1965).

> domestic tax statutes and an income tax convention between the two countries in such a way as to reduce the aggregate of taxes paid to a level below that which would prevail if the activities were conducted entirely in either one of the countries party to the convention. A further example is the establishment of a similar subsidiary by an enterprise of a third state in order to take advantage of the treaty between the two contracting states... *It is the view of the United States Delegation that income tax conventions should be so constructed that they cannot be availed of to avoid legitimate tax burdens, that artificial transactions and business structures entered into or established to avoid legitimate tax burdens should be discouraged and prevented, and that international co-operation to this end is possible and necessary*. (Emphasis added.)[73]

The establishment of a Working Party (WP) was further recommended by the United States Delegation in a second note of 4 January 1962, where it was stated that:

> *... Developments in recent years, however, suggest that income tax conventions must also deal with the problem of legal avoidance of tax achieved through what many regard as abuse of tax conventions*. The experience of the United States, as well as of other countries, has shown that in many cases the tax conventions have been employed for purposes other than the intended objective of eliminating double taxation, and have served as a means by which taxpayers avoid their proper tax burdens. *Through the establishment of related corporations in several countries, often for no purpose other than the anticipated tax benefits, taxpayers in treaty countries have taken advantage of international tax agreements and the interaction between such agreements and internal laws so as to subject their total profits to taxes far below those imposed on purely domestic enterprises in any one of the countries in which these inter-related companies are created. Moreover, residents of non-treaty countries have been able to obtain the benefits of the conventions between two treaty countries by forming corporate entities in one or more treaty countries for the sole purpose of obtaining such treaty benefits.* In both types of cases, benefits are obtained which were never intended by the Contracting States when the tax conventions were negotiated. *The tax avoidance achieved in this manner, legal though it may be, may have serious repercussions. Not only are Governments denied legitimate revenues and inequities created among taxpayers similarly situated, but significant distortions may result in the international allocation of resources...* (Emphasis added.)[74]

WP No. 21 on Tax Avoidance was thus created two weeks later on 17 January 1962 after solicitation by the US Delegation. According to the draft terms of reference, WP No. 21 was requested to consider whether, and to what extent, tax avoidance problems have developed through the abuse of tax conventions between member countries and whether the benefits of a convention should and can be denied to certain entities situated in the territories of the signatories to a convention or in the territories of third countries in order to prevent such abuse. Mr. Gordon, Mr. Ross and Mr. Beinert were representatives of the US delegation (Rapporteur of WP No. 21) together with delegates of Denmark.

What all of this has to do with Italy and precisely with Decision No. 25219 of the CSC? Undoubtedly, the CSC has correctly applied treaty rules and domestic law and its results are also consistent with its previous case law. However, there is a key paragraph in the decision, with which the authors do not agree. As mentioned in section 2., the CSC held that the fact that the taxpayer did not remit taxes in Germany on the capital gain realized on the sale of shares of C.M. srl is not a paramount reason to prevent the application of treaty provisions on the allocation of taxing rights, thus implicitly tolerating situations of double non-taxation. In the authors' opinion, this excerpt reveals itself to be, as a matter of fact, inconsistent with one of the two pillars of the international tax regime, i.e. the single tax principle. In this case, since the primary jurisdiction that had the right to tax – Germany as residence state – refrained from doing so, the other jurisdiction – Italy as source state – should have taxed instead in order to prevent double non-taxation. From a policy perspective, the complete distributive rule of article 13(4) of the Germany-Italy Income and Capital Tax Treaty (1989) made sense at the time that the tax treaty was being negotiated. Indeed, at that time both countries adopted the imputation system under which realized capital gains of corporations were fully taxed. But since both Germany and Italy adopted the participation exemption in 2000 and 2004, respectively, thus exempting capital gains, maybe it is worth suggesting a review of the allocation of taxing rights under article 13 of the OECD Model.[75]

Decision No. 25219 raises interesting questions regarding the international tax regime and the single tax principle. For example, does the single tax principle only relate to juridical double taxation or also to economic double taxation? One can argue that participation exemption systems ensure the single tax principle on the assumption that gains reflect accumulated undistributed earnings (which increase share values) that have already been subject to tax at the level of the investee company. Therefore, an additional tax should not be levied at the shareholder level when stock is sold. Limiting source taxing rights under residence-only distributive rules does not make sense at all when the majority of countries have converged towards exemption for corporate dividends and gains. Indeed, the exclusion of source taxation of capital gains on shares made by non-residents might be subject to abuse by base company practices, leading to double non-taxation. When in 1962 the delegate for Switzerland, Rapporteur of WP No. 19 on the Taxation of Capital Gains, dropped the general policy principle that gains on assets should be subject to the same treaty taxing rules as income from the assets, thus endorsing the approach of residence only taxation for shares that were not the property of a PE, one likely argument, according to Vann, was, "the general problems of reconciling company and shareholder taxation and the variety of systems in different countries that had made the work on the dividends article difficult".[76]Nowadays, where the majority of countries have integrated company and shareholder taxation

73. OECD Fiscal Committee, Note by the United States Delegation on Tax Avoidance through the Improper Use or Abuse of Tax Conventions (14 Nov. 1961), TFD/FC/135, available at http://www.taxtreatieshistory.org/ .
74. OECD Fiscal Committee, Note by the United States Delegation on Tax Avoidance through the Improper Use or Abuse of Tax Conventions (4 Jan. 1962), TFD/FC/136, available at http://www.taxtreatieshistory.org/ .
75. G. Maisto & J. Malherbe, *General Report*, in Maisto ed., *supra* n. 8 .
76. R.J. Vann, *Transfer of Shares and Anti-Abuse under the OECD Model Tax Convention*, in Maisto ed., *supra* n. 8 .

through participation exemption systems, the authors suggest abandoning complete distributive rules, such as article 13(5) of the OECD Model, which allocates exclusive taxing rights to the residence state. In this regard, the proposal of the Dutch delegation of allowing source taxing rights for the sale of predominant interests in companies by non-residents should be re-evaluated.[77] In the meanwhile, if Italian tax policy is to not give up its power to tax in those situations of double non-taxation in order to enforce the single tax principle, the only possible solution would be to renegotiate the Germany-Italy Income and Capital Tax Treaty (1989) and insert a subject-to-tax clause along the lines of that included in the France-Italy Income and Capital Tax Treaty (1989).

77. *See also* R. S. Avi-Yonah, *Money on the Table: Why the U.S. Should Tax Inbound Capital Gains* (3 June 2011). U of Michigan Law & Econ, Empirical Legal Studies Center Paper No. 11-008; U of Michigan Public Law Working Paper No. 239, available at https://ssrn.com/abstract=1857508 or http://dx.doi.org/10.2139/ssrn.1857508 , where the first author argued that Congress should adopt the 1992 Rostenkowski proposal imposing US capital gains tax on foreign sellers of large blocks of shares.