

Proof of tax residence and beneficial owner status for reduced withholding tax

Dr Sergio Finulli



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by **Dr Sergio Finulli**



In European Union countries, the application of the provisions set forth in double taxation treaties has become an issue that must be addressed by the directors of subsidiaries. In the case of EU member states, this is also true with respect to applicable directives which provide for a reduction in the amount of withholding taxes payable to tax authorities when paying foreign dividends, interest, and royalties to foreign companies,

This issue is of particular

importance in countries such as Italy, where the responsibility for applying reduced withholding taxes falls on subsidiaries and their directors.

The background to this stems from the 2019 Danish cases, in which the Court of Justice of the European Union (CJEU), departing from its previous position, clarified that the benefits of the directives do not

apply when the receiving company is merely a conduit company or when the structure constitutes an abuse of law.

With reference to interest and royalties, this conclusion relates to the concept of the beneficial owner; and with reference to dividends, the same logic applies through the anti-abuse clause of the Parent-Subsidiary Directive and its evolution, even

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after the 2015 amendment.

Over the past two years, the Italian Supreme Court has clarified the criteria that must be met in order to qualify for the benefits (reduced rates or exemptions) provided for in treaties and directives.

First of all, tax residency can generally be proven through official documentation (e.g. a

certificate of tax residence issued by the foreign tax authority) provided that it is accurate, consistent, and covers the correct time period.

Determining the ultimate beneficial owner, on the other hand, requires economic substance, autonomy, the ability to retain income, and the absence of mere transit mechanisms. It is here that the true viability of the claim for a reduced tax rate or exemption is at stake.



In one of its most recent rulings on the matter, the Italian Supreme Court emphasised the actual operational activity and financial soundness of the company receiving dividends, interest, or royalties, as evidenced by the financial statements and related report

submitted by the taxpayer as well as the number of employees.

This made it possible to rule out the likelihood that the company receiving dividends, interest, or royalties was merely an intermediary or lacked actual

operational activity. As such, it was not the actual recipient of the payments to which the preferential treatment provided for in the double taxation treaty had been applied.

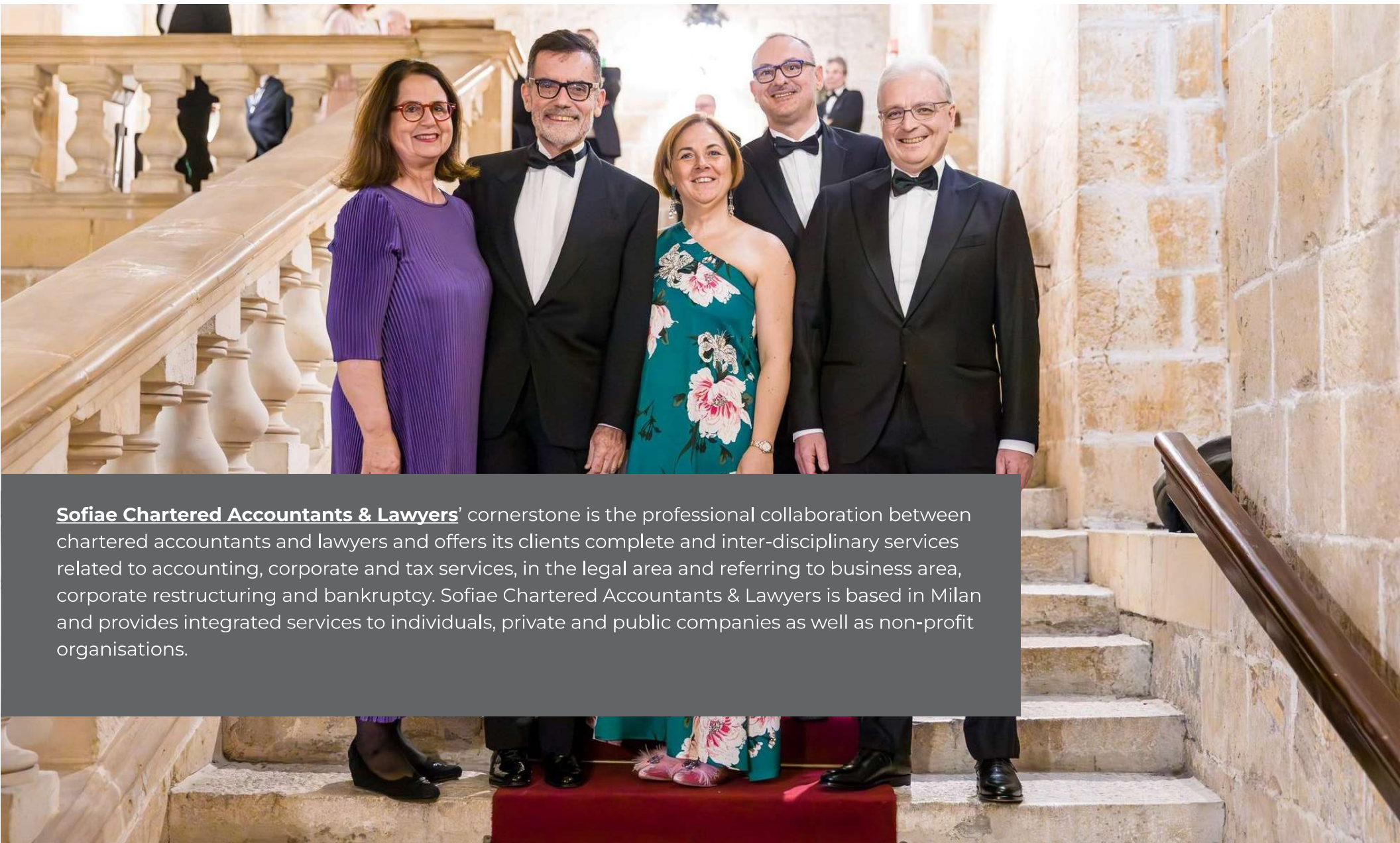
According to the rulings of the Italian Supreme Court, the

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burden of proof regarding the proper application of benefits under double taxation treaties and EU directives lies not with the tax authorities but with the subsidiary paying dividends, interest, or royalties, and such proof must be provided for each tax period.



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