ANSWERS TO THE QUESTIONNAIRE AND SPECIAL REPORTS
ON THE INTEREST SAVINGS DIRECTIVE

by Giuseppe Marino (‘) and Giuseppe Melis (” (”) (***)

II. Questions of policy.

1) Although the ultimate goal of the interest savings directive is to concentrate taxation of interest in the country of residence, the directive does not propose any measure neither to eliminate all withholding taxes in the country of source, nor to impose a tax credit for the elimination of double taxation in the country of residence. Do you see from a policy point of view any justification for this omission?

Directive n. 2003/49/EEC (the “Directive”) aims to concentrate taxation of interest in the country of residence, but it does not aim to allocate taxing rights, nor to “change” internal tax systems. This Directive does not in fact have a purpose of “tax harmonization”, but rather of “tax coordination”, in order to preserve national tax systems and avoid tax evasion on interest.

In order to pursue this aim, the State of residence must be put in the condition – through the exchange of information system – to tax interest received abroad by its own residents. Where this exchange of information is not possible because of hindrances deriving from the particular nature of some legal systems (e.g. States where bank secrecy is considered to be a principle of constitutional Law), interest has to be taxed in the State of source with a final withholding tax, a part of which must be attributed to the State of residence.

With only this last exception, nothing changes in national tax systems of Member States. Each can then choose its own level of taxation on interest paid both to residents and to non residents and is not obliged to give any foreign tax credit. It must however be noticed that an ordinary foreign tax credit provision can generally be found in national legislations of Member States or in double taxation conventions.

So, in conclusion, the circumstance that the Directive does not set any measure neither to eliminate all withholding taxes in the State of source nor to impose a full tax credit in the State of residence, is not to be considered an omission, but a mere consequence of the balance between the Member States’ rights to apply a certain tax

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(*** ) Questions of policy (II, with the exception of n. 8) and question of implementation (III) have been answered by Giuseppe Melis; par. II n. 8, unresolved legal questions (IV), question of withholding and retention tax (V) and question of tax planning and tax avoidance (VI) have been answered by Giuseppe Marino.
policy and the cooperation against tax evasion. To sum up, a measure of “tax coordination”.

2) By concentrating the taxation of interest in the country of residence the interest savings directive is eliminating tax competition on this category of income between the country of residence and the countries of source. Is the idea of eliminating this type of competition by giving a decisive tax advantage to the country of residence, compatible with the rules of the single integrated market and in particular with the free movement of capital, or could the elimination of this type of competition be justified by the fact that it is harmful tax competition?

First of all, this does not seem to be a problem of free movement of capital. We do not agree with those who have spoken of a “tax lobby” of Member States. The residence principle (or “worldwide” taxation) is a general principle applied in all Member States. The savings Directive is just trying to apply this principle to taxation of interest (1). Secondly, this mechanism is a way to cope with the problem of zero (or very low) taxation which some Member States only apply on interest paid to non residents, which can be considered as a “harmful tax measure”, having the only aim to attract financial investments made by non residents.

3) Apart from obvious budgetary reasons for some Member States, what is the justification for exclusive taxation in the state of residence, when many Member States have introduced a dual tax system in which capital income like interests are subject to a proportional rather than a progressive tax?

The principles of personality and progressivity of taxation are stated by art. 53 of the Italian Constitution. The first principle means that taxpayers must be taxed according to their “ability to pay”, which is represented, in case of a tax on income of individuals, by their whole income. The second principle means that the tax system must be built according to a principle of “progressivity”: that means that also proportional taxes are compatible with Italian Constitution, as long as the system as a whole remains “progressive”. In Italy, the income tax on individuals (Irpef) is a personal and a progressive one. However, there are some exceptions. Among them, income deriving from interest is the main one, since it is taxed with a final withholding tax.

The fact that the whole area of income deriving from interest is excluded from the principle of progressivity has been criticized. However, this exception is considered necessary, because of the high mobility of such kind of income. Moreover, the application of a proportional withholding tax simplifies the tax assessment activity and consequently the effectiveness of taxation.

However, personality and progressivity are at two different levels. So, the fact that interest is not taxed in a progressive way does not mean that the State of residence has no power to tax that interest, as, if this were the case, it would, from the Italian perspective, raise an issue of discrimination between Italian residents producing income only in Italy and Italian residents producing income abroad (²).

4) The final objective of the directive is to tax all interest income in the state of residence of the beneficial owner. Now that the state of residence has all the information with respect to foreign source interest income, shouldn’t the directive provide for a mandatory credit eliminating all double taxation, thereby indicating which direction the ECJ should take in cases involving the free movement of capital (either elimination of all taxation at source, or mandatory credit for foreign source interest income)?

According to the Directive, interest has to be taxed in the resident State, without caring about double taxation. A full tax credit should only be granted for the withholding State levied in those States who are allowed not to send information. Nothing is thus provided for other cases.

For this reason, the Directive just preserves financial interests of Member States and it is not addressed to individuals: the aim is thus not to grant free movement of capital.

For this reason, there is no need to provide for a mandatory credit and thus to opt for the application of a “capital export neutrality” principle.

If this is true, it is also true that also individuals’ rights must be taken into account. Since a minimum level of taxation on interest paid to resident is applied all over the European Union, the risk to be taxed twice is in fact very high. On the other hand, the residence State can not be obliged to grant a full tax credit in any case (that is, also in the cases where the withholding tax is not imposed by the Directive and in which a part of this withholding tax is not paid from the source State to the residence State), nor can it be forbidden to the State of source to tax interest paid to non resident taxpayers.

(²) G. Stefani, Conseguenze della globalizzazione sui sistemi tributari, in Boll. trib., 2006, p. 201 ss.
For this reason, a compromise would be the allowance of at least an ordinary tax credit, which however does not fully fit with the residence principle (which would require the full tax credit) (3).

5) In accordance with the OECD model treaty, third countries will maintain their withholding taxes in their relationship with Member States of the E.U. However some Member States grant ordinary tax credits for withholding taxes paid on interest received abroad, whereas for interest received from a Member State under the Interest Savings Directive a full and refundable credit will be available (art. 11 ISD). How will this discrepancy affect E.U. residents in deciding on investment opportunities on third countries compared to investment opportunities within the E.U.?

In the relationship with the States obliged to impose a withholding tax (first group of States), the full tax credit makes the level of taxation equal to the one in the State of residence. It then follows that residents of the residence State are not interested to invest in another State only for tax reasons.

In the relationship with other States (second group of States), assuming that an ordinary tax credit is granted according to national law or to DTC, the final level of taxation depends on the level of taxation of the State of residence and of the State of source. If the level of taxation in the first State is higher than the level in the second one, the final level will be that of the State of residence; in the second case, the final level will be that of the State of source.

In conclusion, the only hypothesis of distortion will be the one in which the withholding tax in States belonging to the second group is higher than the one existing in States belonging to the first group. The fact that according to the Directive the withholding tax of the first group must be at least of 15%, makes however this hypothesis very rare. In any case, the differences on the taxation of interest are very low among different States, which makes the problem not so dramatic.

6) The interest savings directive introduces the principle that one Member State is somehow responsible for the correct enforcement of the tax law of another Member State, by providing it automatically with the correct information on a particular category of income. Is it a principle of international tax law that one country should be responsible for the correct enforcement of another country’s tax laws? If not, is this a principle that is necessary for the operation for the fully integrated single market in the E.U.?

(3) V. Ceriani, Tendenze internazionali nella tassazione del risparmio, in Rass, Trib, 2004, pag. 1375.
As it is known, no international tax law principle provides that one country is responsible for the correct enforcement of another country’s tax laws and no similar principle exists in the Italian Constitution or in Italian tax law. That means that in principle Italy is not obliged to cooperate; this duty is outlined only under the Directive (4).

However, cooperation among States on exchange of information and on assistance on tax collection has developed under both international and European Law. In particular, in the EC this aspect has been widely developed under the so called “global approach”, according to which the EU policy in “tax coordination” must take into account also financial interests of Member States and not only the rights of taxpayers. Moreover, it must not be forgotten that the ECJ has often invoked the existence of the Directive on mutual assistance against Member States, which has been considered by the Court as a way to grant collection of taxes without making use of less proportionate hindrances to taxpayers contrary to the principle of non discrimination or to the exercise of the freedoms granted by the Treaty (5).

7) The interest savings directive is part of a wider objective to balance the tax burdens between income from labour and income from capital. In this perspective, shouldn’t the directive be extended to the payment of all categories of income from capital by individual taxpayers (dividends, royalties, rental income, capital gains on financial assets and payment of private extra-legal pensions, the latter as a solution to exit taxes)? What are the arguments in favour and against such an extension?

The implementation of the free movement of capital has implied the possibility for the taxpayer to make use of capital in other Member States for any kind of investment: i.e. shares out of which dividends are distributed, real estate producing rental income, etc. (6). However, it is difficult to extend the new regime to all kind of income deriving from capital investments. First of all, national legislation provides a special tax treatment for certain types of income due to social policy reasons. This happens, for instance, with payments of private pensions, which follow different schemes of taxation aimed at stimulating individuals to save money for private social security. Under this perspective, the receipt of an

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(4) On international tax law principles, see C. Sacchetto, Le fonti del diritto internazionale tributario, in Corso di diritto tributario internazionale coordinato da V. Uckmar, Padova, 2002, p. 44.

(5) See, for instance, Bachmann case, Halliburton case, Baxter case and Schumacher case.

interest on a capital and to receipt of a sum aimed at integrating public pensions are quite different facts.
Secondly, the taxation of some types on income should be seen in a more complex way. For instance, the taxation of dividends is strictly linked to double economic taxation issues, so that it cannot just be solved through a minimum withholding tax.
Finally, interest constitutes for individuals a “net” income, on which a withholding tax can be easily applied. This is not true for every type of income. E.g.: in rental income some kind of expenditures can be deducted from taxable income; deductible costs for research and development of intellectual property giving rise to royalties can be different across the Member States (for instance, in Italy there is a deduction of 25%).

8) Are the present guarantees with respect to the exchange of information provided for by the U.S. satisfactory or should the E.U. insist on exchange of information upon request as defined in the OECD Model Agreement for interest payments and what would be the difference with the actual U.S. practice?

As far as the actual US practice about exchange of information is concerned, it must be noted that the savings directive does not become fully effective until the EU Council is satisfied that the United States is committed to exchange of information on request with respect to interest payments to residents of the EU Member States. Whether the US will exchange information on request is doubtful. There have been several proposals in this respect.
In January 2001, the US Internal Revenue Service issued proposed regulations that would have required reporting of all bank interest payments to non-resident aliens. The regulations were replaced in 2002 with proposed regulations under which it would only be necessary to report such payments made to individuals residing in several States (i.e., Australia, Denmark, Finland, France, Germany, Greece, the Netherlands, Ireland, Italy, New Zealand, Norway, Portugal, Spain, Sweden, United Kingdom, and the Canada). The reporting of payments made to residents of the 12 EU Member States was proposed in order to satisfy the savings directive’s requirement that the US exchange information. Nowadays, the US seems not to be favourable to the idea of helping the EU implement the Saving Directive, which has been implemented for European purposes only.
The ECOFIN Council concluded (at its meeting of 21 January 2003) that the requirement that the United States apply “equivalent measures” to those in the Saving Directive was “effectively satisfied”.
Thus, the exchange of information provided for by the U.S. is considered satisfactory for the purposes of the savings directive implementation. However, it seems that the US will not implement a system of automatic exchange of information. Nevertheless, it must be underlined that the US has no obligation to cooperate in order to develop the internal EU market. It must be noted that, the United States has implemented its own method of getting information on savings held abroad by its citizens and residents. Under US law, financial institutions outside the United States that are “qualified intermediaries” (QIs) are required to know the identity of the actual owners of their accounts. If any of an institution’s accounts are held by US citizens or resident aliens, the institutions must either file information reports with the IRS or withhold tax from the accounts. This reduces the pressure on the US to cooperate with the EU as a means of protecting its own revenues.

9) The directive provides several ways and means to submit evidence of residence and payment of interest. Shouldn’t there be a standardized way, for example a standardized certificate of residence?

The Directive provides several ways to submit evidence of residence, referring to identity cards and passports, tax identification numbers and any other documentary proof of identity. These documents can provide evidence of the taxpayer’s residence. However, the legislation of the various Member States is different with reference both to the issuing of said documents and to the duties to keep them updated. Therefore, problems in the certification of the residence may arise. These documents constitute a valid presumption since the introduction of a standardized certificate could be difficult; such certificate would indeed need to be a certificate that each taxpayer can easily obtain. It must be considered that the effectivity of the Directive is related to the possibility to obtain the information required easily.

III. Questions of implementation.

Before the questions below are answered, please provide with regard to your country a ‘Brief overview’ on the following aspects:

a. the taxation in your country of interest income earned by resident and non-resident individuals as (i) business income and (ii) income from private investment (withholding, preferential taxation (‘dual income system’), taxation on aggregate income, deductions, rates etc.), and
b. an overview of typical special provisions in your country’s tax treaties with respect to interest income (cf. Article 11 (Interest) of the OECD Model)

a) Taxation in Italy of interest income earned by resident and non-resident individuals as:

<table>
<thead>
<tr>
<th>(i) Business income</th>
<th>earned by a resident entrepreneur</th>
<th>earned by a non-resident entrepreneur</th>
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<tbody>
<tr>
<td>Interest of any kind</td>
<td>is part of the whole business income (Art. 48 , CAIT)</td>
<td>is always considered as capital income, being the existence of a permanent establishment only relevant in case of companies (art.48, CAIT). See thus the scheme for interest from private investments</td>
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<th>(ii) Interests from private investments</th>
<th>earned by a resident individual</th>
<th>earned by a non-resident individual</th>
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<tbody>
<tr>
<td>deposit accounts and current accounts with banks and post offices (⁷)</td>
<td>27% final withholding tax (Art. 26, co. 2, d.P.R. 600/73)</td>
<td>Exempted (Art. 23, co. 1, lett. b), CAIT, art. 26, co. 2, lett. b), d.P.R. 600/73)</td>
</tr>
<tr>
<td>Interest and loans, deposits and current accounts revenues.</td>
<td>12,50% withholding tax (Art. 26, co. 5, d.P.R. 600/73)</td>
<td>Exempted if the state of the receiver applies the exchange of information, otherwise 12,50% final withholding tax (27% final withholding tax if the receiver is resident in a tax haven) (Art. 26-bis, d.P.R. 600/73, art. 6, d.lgs. 239/96)</td>
</tr>
<tr>
<td>Bonds issued by listed companies and having a duration exceeding 18 months, State debts and similar securities (⁷)</td>
<td>12,50% final withholding tax (art. 1, d.lgs. 239/96)</td>
<td>Exempted if the state of the receiver applies the exchange of information, otherwise 12,50% final withholding tax (art. 6, d.lgs. n. 239/96)</td>
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<tr>
<td>Bonds issued by non listed companies</td>
<td>12,50% withholding tax or 27% withholding tax Based on the expiring date (exceeding or not exceeding 18 months) (Art. 26, co. 1, d.P.R. 600/73)</td>
<td>12,50% withholding tax or 27% withholding tax Based on the expiring date (exceeding or not exceeding 18 months) (Art. 26, co. 1, d.P.R. 600/73)</td>
</tr>
<tr>
<td>Interest and revenues from securities different from shares and similar securities</td>
<td>27% final withholding tax (Art. 26, co. 1, d.P.R. 600/73)</td>
<td>27% final withholding tax (Art. 26, co. 5, d.P.R. 600/73, artt. 5, 6, 7, 8 d.l. 512/83)</td>
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</table>

(⁷) Interests are taxable in Italy if they are paid by resident natural or legal persons (artt. 23, co. 1, lett. b, CAIT).
(⁸) Such income can be taxed in accordance to a special regime (the so called “regime del risparmio gestito”): such regime is applicable provided that the participations are managed by an authorized financial operator entrusted by the taxpayer. Such financial operator managing the portfolio applies a 12,50% final withholding tax to the accrued positive earnings of the portfolio. According to such regime the taxpayer does not need to file a tax return with respect to these incomes, moreover revenues are taxed when accrued and not at their realization (art. 7, d.lgs. n. 461/97).
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<tr>
<th><strong>Revenues deriving from sale and repurchase agreements, swaps (i)</strong></th>
<th><strong>12.50% final withholding tax (Art. 26, co. 3-bis, d.P.R. 600/73)</strong></th>
<th><strong>Exempted if the state of the receiver applies the exchange of information, otherwise 12.50% final withholding tax (27% final withholding tax if the receiver is resident in a tax haven) (Art. 26-bis, d.P.R. 600/73, art. 6, d.lgs. 239/96)</strong></th>
</tr>
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<tbody>
<tr>
<td><strong>Revenues from guaranteed securities loan</strong></td>
<td><strong>12.50% final withholding tax (Art. 26, co. 3-bis, d.P.R. 600/73)</strong></td>
<td><strong>Exempted if the state of the receiver applies the exchange of information, otherwise 12.50% final withholding tax (27% final withholding tax if the receiver is resident in a tax haven) (Art. 26-bis, d.P.R. 600/73, art. 6, d.lgs. 239/96)</strong></td>
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<tr>
<td><strong>Other interest and revenues deriving from the investment of capital</strong></td>
<td><strong>12.50% withholding tax (Art. 26, co. 5, d.P.R. 600/73)</strong></td>
<td><strong>12.50% withholding tax (Art. 26, co. 5, d.P.R. 600/73)</strong></td>
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No withholding tax is levied on interest paid to non-resident entities on:

1. deposit accounts and current accounts with banks and post offices;
2. bonds issued by the state, banks or listed companies, if paid to:
   
   a. foreign central banks and bodies investing the public reserves of the foreign country;
   b. residents of countries that allow the exchange of information, with the exception of countries or territories outside the European Union with a preferred tax regime (see below); or
   c. institutional investors (e.g. funds), whether or not subject to tax, established in countries that allow the exchange of information, with the exception of countries or territories outside the European Union with a preferred tax regime (see below); and
3. deposit accounts and current accounts, not being cash loans, with debtors other than banks and post offices (e.g. intercompany current accounts and intercompany deposits) if paid to recipients mentioned under (2) above.

In order to benefit from the exemption under (2), the non-resident must deposit the bond with a resident bank or other approved intermediary.

Interest on bonds other than those mentioned under (2) are subject to withholding tax. The rate is generally 27%. A 12.5% rate applies to interest on bonds with a maturity of at least 18 months, provided that, at the date of issue, the interest rate was not higher than (a) 200% of the official discount rate, in the case of bonds listed on an EU regulated market or (b) 166% of the official discount rate, in the case of other bonds. Interest on public and private bonds issued before 1 January 1997 may be subject to other rates.

Interest on deposit accounts and current accounts other than those mentioned sub (1) and (3) is subject to a 27% withholding tax.

Other types of interest paid to non-resident companies, including interest on loans, are subject to withholding tax at a 12.5% rate (27% if paid to a resident of a country or territory outside the European Union with a preferred tax regime). The withholding tax on payments to non-resident companies is always a final one (i).

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b) Overview of typical special provisions in Italian tax treaties with respect to interest income.

*Italy does not have its own model treaty but it refers to the OECD Model Convention, selecting the provisions from one version or the other. The article on permanent establishment is normally derived from the 1963 version. However, with respect to dividends, interest and royalties, the concept of "beneficial owner" is usually derived from the more recent treaties. One deviation from the OECD Model Convention is that Italian treaties normally also maintain taxation in the source state for royalties. As far as interest is concerned, tax treaties signed by Italy generally follow article 11 of the OECD Model.*

*Italian treaties do not normally contain a limitation on benefit clause, although there are exceptions (e.g. the protocol to the Italy-United States treaty). Specific anti-abuse clauses are present in several articles of the treaties (\(^{10}\)).*

1) Did you country implement the interest savings directive, fully or partially?

*Italy has implemented the Directive with law decree 18 April 2005, n. 84 (the "Decree"). The Italian Tax Administration then added some clarification with two formal acts on 8 July 2005 (concerning the technical aspect of the exchange of information between the paying agent and the Italian tax authority, implementing art. 6 of the Decree, and the formal request that residual entities must file in order to be treated as a harmonised UCITS (art. 4, par. 3, of the Directive), implementing art. 1 of the Decree - see question 5); a third one on 25 July 2005 (concerning the formal request through which an Italian beneficial owner can certify his status, implementing of art. 9 of the Decree) and a circular letter (30 December 2005, n. 55, from now on the "Circular") which contains some formal clarification on the content of the Directive.*

2) In implementing the interest savings directive, did the implementing legislation just refer to the directive and incorporate it into national legislation as a whole, or was specific national legislation developed for the implementation?

*A specific national legislation has been developed for the implementation. Some parts of the Decree however directly refer to the directive itself.*

\(^{10}\) M. Piazza, *Guida alla fiscalità internazionale*, Milano, 2004, pag. 577
3) When specific national legislation was developed, did the national legislator use identical concepts (interest, beneficial owner, paying agent etc.) as in the directive, or are there deviations from the directive? You can answer those questions in detail in one of the other questions below referring specifically to these concepts?

As we will see in the following questions, the Italian legislator uses the same concepts outlined by the Directive. However there are some differences due to changes that were necessary in order to adapt the European concepts to the Italian ones (11).

4) Beneficial ownership is a central concept in the directive. Is there a concept of beneficial ownership in your national tax system and/or tax treaty system and how is it structured? How does it apply to concepts such as trusts (discretionary trusts and other forms of trusts, Stiftungen), foundations and other similar forms of intermediaries?

No, there is no national concept of beneficial ownership in the Italian tax system. In tax treaties, Italy refers to the OECD model convention and to its commentary (12).

Consequently, in implementing the Directive, Italy referred to the Directive concepts. According to art. 1 of the Decree a subject is considered to be the beneficial owner of the interest if he is the “final beneficiary” of such interest.

The Circular (point 1.1) states that a beneficial owner is a physical entity, resident in a Member State, that receives interest payments by a paying agent resident in a different Member State. Corporate entities are not included in the above definition of beneficial owner, since the Directive only applies to individuals.

Moreover, for the sake of simplicity, the beneficiary of an interest payment is always considered the beneficial owner of such interest, unless he proves that he was not.

It may happen that an intermediary is considered transparent for tax purposes. In such hypothesis, even if the intermediary receives the interest, he is not considered as the beneficial owner.

5) Paying agent is a central concept in the directive. Is there such a concept in your national tax system and has it been used for the


implementation of the directive, or did your country develop a new concept, or amend the existing concept?

The paying agent should be identified as the last intermediary making the payment of interest in favour of the effective beneficiary. Art. 1 of the Decree (and art. 1, point 1, statement of 8 July 2005 implementing art. 6 of the Decree) outlines the category of subjects, Italian residents, that, acting as paying agents, shall notify the Tax Authorities all information related to interest paid directly to individuals that are the effective beneficiaries and that reside in a different Member State. Among paying agents the Decree include the following:

- Banks
- Financial companies
- Italian Mail Company ("Poste Italiane S.p.A.")
- Saving management companies ("società di gestione del risparmio")
- Fiduciary entities
- any other entity, including individuals, that for professional or commercial reasons pays interest to non resident individuals being the effective beneficiaries of the same;
- Italian permanent establishments of foreign entities similar to those above listed.

Notifications shall be due not only when the paying agent acts as the direct debtor of the interest paid (e.g. when he is the issuer of the bond), but also when he is entitled to pay interest on behalf of a different debtor or when he is acting on behalf of the beneficiary. In case the paying agent is not paying interest on its own behalf, in order to qualify as paying agent he should bear an entitlement to do so by either the debtor or the beneficiary of the interest.

According to the Directive, art. 1, para. 3, of the Decree specifies that also residual entities, which are the beneficial owners of interest payments or receive an interest payment on behalf of a non-resident beneficial owner, must comply with notification duties at the time of the payment, provided that such entities are not corporate entities or entities whose income is taxed as business income or an harmonized UCITS entity. According to Italian law, “residual” entities are:

1. non-commercial entities such as committees, associations and foundations; partnerships and similar entities according to art. 5 of Italian Consolidated Act on Income Tax – CAIT –.
2. De facto partnerships whose scope is the exercise of commercial activities and associations without legal personality created by physical persons for the exercise of intellectual activities are considered as partnership.
3. Italian investment entities operating in the investment products which are not authorised according to Directive 85/611/CE;
4. trusts, constituted according to articles 10 and 11 of Aja Convention of 1 July 1985, ratified in Italy with Law 16 October 1989,
n. 364, not exercising commercial activities, with administrative seat or main object of activity in Italy.
Pension funds, insurance entities and real estate funds (see Decree illustrative report) are not considered as residual entities. Residual entities must comply with all notification duties outlined for intermediaries, indicating the beneficial owners (i.e. their shareholders/beneficiaries/etc.) of the payments in case such entities are physical persons who reside in other EU Countries, irrespective of the effective payment of such interest to their beneficial owners. Then, at the effective payment of the interest no notification obligation shall be, therefore, complied with.
Such entities may also opt, for the sole purposes of the Directive, to be treated as a harmonised UCITS (art. 4, para. 3 of the Directive) filling, as required by art. 1, para. 4, of the Decree, a specific form whose content is outlined by 8 July 2005 statement implementing art. 1 of the Decree.

6) Interest is a central concept in the directive. Does the concept of interest of the directive coincide with the concept of taxable interest in your country and if not in what way do the two concepts vary?

The definition of “interest payment” provided by the Directive and by the national legislation does not refer to the Italian tax meaning of interest \(^{(13)}\) as it can be inferred from tax legislation (art. 44, CAIT). On the contrary it provides for a specific case of earnings to be taken into consideration.
The wording “interest payments” definitely include earnings deriving from any kind of relationship (either securitized or not) that grants third parties the right to of a capital that shall later be refunded. The legislation refers to “interest related to credits having any kind of nature” and to interest related to public debt and other bonds.
More in detail, art. 2, para. 1, letter a) of the Decree implementing the Directive states that interest payments that shall be notified are the following (when defining credits, the Decree refers to the OECD double tax treaties definition of the same):

- interest on credits having any kind of nature;
- accrued interest realized at sale, refund or redemption of such credits;
- income distributed by common investment institutions trading in securities (UCITS) authorized to operate according to Directive 85/611/CEE (so-called "harmonized"), by certain common saving investment institutions (OICR) and by other entities called "remaining entities";

income realized at sale, refund or redemption of participations or quotas of said investment institutions and entities in case they invest more than 40% of their assets in credits included in the Directive definition. Since 1 January 2011 such 40% percentage will be reduced to 25%.

As specified in art. 2, para. 1, letter a) of the Decree, items that shall be notified are "interest paid or credited on an account and related to credits of any nature, either guaranteed or not by a mortgage and either having a participation to the debtors' profits clause or not, more in detail those interest linked to public debt and those earned on bonds, including other earnings deriving from such securities or bonds" (see also art. 6 of the Directive).

Such a definition of interest is extremely wide and does not indicate a specific "cause" of the credit, nor the "quality" of the debtor (that can therefore be a private or public entity, either exercising or not a business activity), nor does it indicate the debtor's residence (EU or extra-EU). Moreover, interest - directly paid or credited into an account - can be related to a guaranteed credit or to a non guaranteed one and can also require the debtor to pay a profit.

On the contrary, interest and other proceedings deriving from bonds, including public debts, are explicitly mentioned, with the only exception of bonds to which the Directive is not directly applicable due to the "grand fathering clause".

Interest to which the Directive refers to are only those that can be defined as a "consideration", i.e. those that represent an earning deriving from the investment of a capital. Art. 1, para. 1, letter a) of the Directive and art. 2, para. 1, letter a) of the Decree, indeed, state that delay interest do not represent payment of interest. This principle is applicable irrespective of the possible qualification of such interest as capital profits according to Italian tax law. According to art. 6, para. 2, CAIT, delay interest and those for delayed payment represent income having the same nature of the credits giving them origin.

Therefore, the following items should be considered:

- interest on loans, deposits, current accounts, either guaranteed or not by mortgage and either consisting or not of securities or certificates;
- interest and other profits deriving from public debt or from bonds and similar securities, including revenues deriving from securities whose profits are linked to certain financial benchmarks;
- interest related to credits or forms of participations in a company's economic result.

Moreover, the Directive is considered to include interest on loans exceeding the "debt to equity ratio" (regulated by art 98, CAIT) and thus qualified as dividends. The above criterion has been chosen by the Italian legislator in order to facilitate paying agents' duties, although it allows the inclusion within the scope of the Directive of interest payments that should be excluded.
Profits deriving from deposit certificates, saving bonds ("buoni fruttiferi"), irrespective of their duration, as well as profits deriving from any kind of security different from those linked to the results of the issuing entity also fall within the scope of the Directive.

As above mentioned, credits may require the debtor to pay a profit to the creditors, i.e. in case of the so called “participative” bonds that do not provide for a similar participation in losses. Italian law qualifies such bonds as shares and applies shares tax regime (art. 44, para. 2, letter a), CAIT).

With respect to this issue, the Decree illustrative report states that “participative” bonds are considered to produce interest and not dividends, except when the creditor actually undertakes the same debtors’ entrepreneurial risks.

According to art. 2, para. 1, letter b) of the Decree, interest accrued at sale, refund or redemption of credits fall within the scope of the Decree/Directive. The Directive illustrative report clarifies that also interest accrued or capitalized at the sale, refund or redemption of zero coupon bonds fall within its scope.

7) How did the national legislator organize the transfer of information by the paying agent to the competent authority of the national tax legislation? Did the national legislator use existing rules with respect to exchange of information between financial institutions and the national tax administration, or have new rules been developed and if so what rules? Have the concrete administrative procedures to provide the information (forms, channels, dates) already been implemented and if so what are the rules?

The Italian Tax Authority with a statement of 8 July 2005 implementing art. 6 of the Decree-outlined the terms, conditions and technical aspects of the relevant notification as follows:

- amount of credited interest, with reference to interest on credits paid or credited on an account;
- entire amount of the sale price or of the amounts paid at refund or redemption, for interest accrued or capitalised at sale, refund or redemption of credits (e.g. interest realized at refund or redemption of zero coupon bonds);
- entire amount of income distributed by harmonized UCITS, by similar entities or by collective investment institution resident outside the EU;
- amount of the sale price or of the amounts paid at refund or redemption, for income realized at sale, refund or redemption of participations or quotas of harmonized UCITS, of similar entities or of collective investment institution resident outside the EU;
- amount of interest attributable to each of the members of an institution different from those listed above and who must fulfil
notification duties for interest paid or credited to a non resident entity that did not opt for the application of the UCITS regime;

- total amount of interest paid or attributed to the entity, the name and address of the entity for interest paid or credited to a non resident entity that did not opt for the application of the UCITS regime.

Art. 6, para. 1 of the Decree and the Tax Authority statement of 8 July 2005 implementing art. 6 of the Decree, outlines the terms and conditions for the notification of the relevant data.
The term to perform the notification of the data regarding a certain fiscal year is 30 April of the following year.
The notification shall be made through the electronic system of Entratel or through Internet (14).

8) How did the national legislator organize the transfer from the national competent authority to the competent authorities of the other Member States? Did the national legislator use existing procedures on the basis of bilateral tax treaties or on the basis of the OECD arrangements on exchange of information, or did he develop specific rules and procedures and if so what are these rules?

Italy arranged the transfer from the national competent authority to the competent authorities of the other Member States just referring to art. 9 of the Directive.
According to art. 7 of the Decree, the tax authority has the duty to pass the information on to the competent authority of the Member State of which the beneficial owner is a resident.
Each Member State shall inform the European Union which is its competent authority. For Italy, the competent authority is the “Agenzia delle Entrate”.
The notification of information is automatic and shall take place before 30 June of the year following the one in which interest is paid.
Italy does not use existing procedures on the basis of bilateral tax treaties nor does it use existing OECD arrangements on exchange of information. Moreover, it has not developed specific rules and procedures.

9) How is the exchange of information organized from one paying agent to another paying agent within the same tax jurisdiction? Did your country develop new rules, or has use been made of existing rules?

(14) According to art. 6, para. 2 of the Decree, in case of omitted, incomplete or incorrect notification of the relevant information a sanction ranging between € 2.065 or € 20.658 will be applied. In case of delayed notification, with a delay not exceeding 30 days, the sanction will be applied at its minimum rate
There is no special rule for the exchange of information from one paying agent to another paying agent within Italy. Moreover, no new rule has been developed and no existing rule has been used.

10) The directive provides for certain forms of evidence to establish the residence of taxpayers. Are the documents mentioned in the directive available and used in your country to determine residence? Do you think there may be other documents or data, used in your country, enabling the national tax administration to establish the residence of a taxpayer?

As previously mentioned, the Directive provides several ways to submit evidence of the residence, in particular it refers to identity cards and passports, tax identification number and any other documentary proof of identity.

Art. 2, para. 2, CAIT sets that “with reference to income tax purposes, a person is resident in Italy if for the most part of the fiscal year such person is included as a resident in the registry office lists or have his habitual domicile within the Italian territory or is resident according to the civil code rules”. The tax rule, therefore, refers both to a formal element, registry office lists, and to the civil concept of domicile or residence, linking these two concepts to the Italian territory; in both cases, moreover, a time limit requirement must be met (“most part of the fiscal year”, i.e. 183 days) (15).

As far as evidence is concerned, Italy permits to determine residence through any of the documents listed in the Directive. In addition, according to Italian tax law, the driving license can be listed among the other documentary evidence. Moreover, every citizen can obtain a certificate which shows his/her residence or can certify under his/her responsibility (including criminal responsibility) his/her residence. All these documents, according to the Directive and to the Decree (and to statement of 8 July 2005 implementing art. 6 of the Decree), can be used both by tax authorities and taxpayers to establish the latter’s residence.

Italian tax law in general does not set limits to prove residence (unless in case of residence in a State with a preferential tax regime), which is in line with the Directive.

11) Is there any provision in your national tax system on matching the tax credit for the special withholding tax, with information on the effective withholding of such tax in the country of source? Can the tax credit for the special withholding tax be taken for the tax year in which the tax was withheld in the country of source?

When implementing the Directive, the Italian legislator allowed the application of the foreign tax credit method according to art. 165, CAIT to avoid cases of double taxation.

The deduction of foreign taxes shall be determined in the tax return referred to the fiscal year in which the relevant foreign income has been included in the tax return, provided that the final payment of such taxes occurs before the final term set for the filing of the tax return. According to art. 165, para 4, CAIT indeed, the tax deduction can be applied only if it is determined with reference to the tax return of the fiscal year in which the foreign income is produced and only if the final payment of the relevant foreign taxes are paid before the filing of the tax return.

In case the taxpayer opts for the calendar year, this implies that, with reference to fiscal year 2004, for instance, foreign taxes can be deducted from IRES although the relevant income has been produced during 2004 in case they are paid before the term for the filing of fiscal year 2005 tax return which is 31 October 2006.

IV. Unresolved legal questions

1) What is in your opinion the legal status of a taxpayer who has been identified as an E.U. resident under the directive and who proves that he is not a resident of a Member State under the rules of international tax law?

Generally speaking, the EU law should prevail on the international law. Moreover, the savings directive and the international tax treaties have different purposes. It must also be noted that, under the savings directive, the paying agent shall establish the residence of the beneficial owner only for directive purposes.

Thus, the determination of the residence for savings directive purposes does not affect the legal status of taxpayers under international law, i.e. under tax treaty law.

Nevertheless, the paying agent shall establish the residence of the beneficial owner by using the information at its disposal. And article 3 par. 3 of the Directive says that he shall establish the residence of the beneficial owner “on the basis of any documentary proof of identity presented by the beneficial owner”.

A taxpayer shall not be considered resident in a Member State, if he can prove that he is not resident in that State. And he can prove that by means of a tax residence certificate issued by the competent authority of the third country (in which the individual claims to be resident).
Thus, the answer seems to depend on the means of proof produced by the taxpayer. The taxpayer has to prove that he is not resident in a member state and that he is resident in another state (member or not).

Thus, if he proves that he is not a resident of a Member State under the rules of international tax law, he should be considered not resident in that member state for the savings directive purposes.

While, if he fails to prove that, he will be considered in a member state for that purposes. But that circumstance does not affect the taxpayer residence status under a tax treaty.

Thus the burden of proof is with the taxpayer who has to demonstrate to the paying agent if he is resident in a member state (different from that known by the paying agent). But he has to prove that by one of the means provided by the savings directive.

From this point of view the directive seems to provide for a wide range of evidences. As mentioned above, art. 3 of the Directive consent to prove the residence on the basis of any documentary proof of identity.

Nevertheless, the tax residence under international tax law does not automatically change the legal status of the taxpayer for the savings directive purposes. He must provide for adequate evidences (documentary proof) of its authentic residence.

On the other hand, the proof of residence for the savings directive purposes does not affect the residence status under the international tax law (e.g. the residence for tax treaties purposes).

Thus, the legal status of a taxpayer can be different under savings directive from that under international tax law. The same is true in respect of the relationship between residence under tax treaties and residence under domestic law.

One may argue that competent authority shall not communicate the information referred to in art. 8 of the Directive to the competent authority of the Member State of residence of the beneficial owner if that State does not tax the income because of a tax treaty.

It must be noted that the aim of the directive is to enable interest payments to be made subject to effective taxation in accordance with the laws of the Member State of residence of the beneficial owner.

The ultimate aim of the directive can be achieved through the exchange of information.

Thus it seems appropriate to communicate the information under the savings directive, even if the State of residence does not levy taxes on the interest payment according to a tax treaty.

Under the directive, the competent authority of the State of residence of the paying agent is not obliged to know if the State of residence of the beneficial owner will levy a tax on interest income. Thus, the competent authority must exchange the information referred to in art. 8 of the Directive, without any consideration to the effective taxation in the other State.
The taxation in the State of residence of the beneficial owner will be based on national tax law and not on the savings directive. Nevertheless, it must be underlined that the directive does not provide for any guidance on the relationship between international tax treaties and the directive itself.

2) If a taxpayer turns out to be a resident of another Member State, than the Member State indicated by the paying agent, what should be done with the information? Should it be forwarded automatically to the authentic state of residence?

The problem is that the State of residence of the beneficial owner is established by the paying agent only on the basis of the information at its disposal. But the taxpayer could turn out to be resident in another Member State, other than that established by the paying agent.

The directive does not cover the case of a taxpayer who is resident in a Member State, other than that communicated by the paying agent. Where the beneficial owner is resident in a Member State, the paying agent must report information to the competent authority of its Member State and the competent authority shall communicate the information to the competent authority of the Member State of residence of the beneficial owner.

Thus, according to the Directive those information shall be forwarded automatically to the state of residence of the beneficial owner indicated by the paying agent.

In other words, the directive does not provide any rules binding the authorities of the State of residence of the paying agent to verify the information provided by the paying agent.

It is understood that those information must be automatically communicated to the “authentic” State of residence.

The State of residence of the paying agent communicates the information automatically to the State that has been identified by the paying agent, on the basis of information at its disposal. Thus the competent authority are not obliged to verify such information. Nevertheless, it should not be prohibited to amend the residence of the beneficial owner, for the purposes of the directive, once that the paying agent has determined the authentic state of residence.

In my opinion, the problem is what should be done with the information communicated to the “wrong” State of residence. Moreover, the savings directive does not cover the obligations of the State that received information from the State of residence of the paying agent.

An important fact to note is that the Directive aim to provoke a great level of transparency in the savings industry. For this reason the information should be forwarded automatically to the authentic state of residence, in order to disclose identity of
individual recipients to their home tax authorities. In other words, it would be a nonsense, in practical terms, if those information should not be communicated to the authentic state of residence, once it had been discovered the authentic residence of the individual recipient.

3) The directive puts the burden of proof for the residence of the beneficial owner entirely on the paying agent, while under treaty law the burden of proving residence in order to reduce source taxation generally is on the taxpayer. Shouldn’t the directive impose duties on the cooperation of the non-resident taxpayer and provide sanctions in the state of residence if the beneficial owner does not cooperate?

The cooperation in the proof for the residence of the beneficial owner could be not efficient. Moreover, it is logical to suppose that the paying agent has all the relevant information in order to establish the residence of the beneficial owner for the directive purpose. The paying agent needs to know its customer. In any case, a minimum of cooperation is also necessary in order to provide the paying agent the relevant documents indicated by art. 3, para 3 of the Directive.

This article says that the paying agent shall establish the residence of the beneficial owner on the basis of the passport, the official identity card or, if necessary, on the basis of any documentary proof of identity presented by the beneficial owner.

It must be noted, that in order to minimize the administrative burden on the paying agents, any individual is regarded as beneficial owner unless he demonstrates that he has not received the interest for his own benefit. Thus, the directive provide for a certain level of cooperation between taxpayer and paying agent in order to identify the beneficial owner. If the directive established a duty of cooperation it could bring to a great burden on the paying agents. The burden of proof is not put entirely on the paying agent, because he has to determine the residence of the beneficial owner using the information at its disposal, i.e. the information of its customer.

The paying agent can identify the residence of the beneficial owner with the information at its disposal without looking for further information or documents.

Nevertheless, it is a burden of the beneficial owner to provide for any relevant information in order to prove its “true” residence. For this reason, the burden of proof is firstly put on the paying agent; the burden of proof is put on the beneficial owner, when he wants to demonstrate a different residence.

In any case, it seems reasonable to assume that the paying agent will ordinarily have at its disposal information about its customer residence. Problems may arise when the authentic residence of the beneficial owner is different from that known by the paying agent and, at the
same time, the beneficial owner does not prove his authentic residence. This “conflict of interest” may provoke a lack of efficiency in the implementation of exchange of information under the savings directive. In order to correctly implement the directive according to its aim it is necessary to determine the effective State of residence of the beneficial owner who receives savings income. Moreover, the directive shall not impose a greater level of cooperation than that provided by national law for domestic tax law purposes. In other words, the beneficial owner shall guarantee the level of cooperation generally requested by the tax law of its State of residence.

Generally speaking, a directive shall not impose a harder burden of proof than that established by the tax law of its State of residence. For this reasons, it seems appropriate that sanctions, in the event that the beneficial owner does not cooperate with the paying agent, are not provided by the directive. Nevertheless, each Member State could provide for sanctions in the event of mis-cooperation, in order to effectively implement the directive.

It must be underligned that it could be very difficult to establish if the beneficial owner cooperates with the paying agent who is resident in another State.

4) The rules with respect to the identification of the beneficial owner are based on the money laundering directive. Will this, in your opinion, result into a confusion regarding the authority to which the information will have to be sent: competent tax authority or money laundering authority? If indeed indicators of money laundering are established is it a good idea to have a criminal investigation on money laundering for concealing payments in the country of source and a criminal investigation for tax evasion in the country of residence?

Exchange of information helps wider compliance with the tax systems of Member States including tackling the serious problem of cross-border “laundering” of the proceeds of tax evasion. This system will often draw the attention of the state of residence to the existence of an asset which may have been funded from gains which have themselves been hidden from the tax authorities or from illicit profits.

If the information can have relevance for the anti money laundering legislation it should be communicate to the competent money laundering authority (for the purposes of domestic anti laundering legislation) and to competent tax authority, for the purposes of savings directive.

Maybe it could provoke confusion in the information communication to national authorities.
Nevertheless it seems useful to use information received under savings directive for anti money laundering activities. It must be noted that the interaction between anti-money laundering legislation is out of the scope of the savings directive. Criminal investigation on money laundering may arise, in the State of source or in the State of residence, following the information exchanged under savings directive. The exchange of information can help in implementing anti money laundering investigation in the case of transnational transactions.

5) Is the information to be provided by the paying agent according to art. 8: identity, residence, name and address of paying agent, amount of interest paid and account number or identification of debt claim in your judgment adequate to allow the tax administration in the state of residence to make an assessment? Is there other information that could be useful in this respect?

The information to be provided by the paying agent in art. 8 of the Directive are, generally speaking, adequate to allow the tax administration in the state of residence to make an assessment, as far as this information refers to the beneficial owner. There may be a sense that exchange of information will become the international rule for cross border income flows. Exchange of information to ensure effective taxation of cross border interest offers a number of advantages, because it encourages compliance with the tax system. In this respect, it could be useful, in order to make an assessment, to communicate the tax code of the beneficial owner in his country of residence.

6) The directive organizes the exchange of information in two stages: (a) information transferred from the paying agent to the national competent authority and (b) information transferred for one competent national authority to another. Would it be more effective to transfer the information directly from the paying agent to the competent national authority of the state of residence, and what would be the conditions for such a transfer to become possible from a legal point of view?

One of the most complex implementation issue is the development by the paying agent of a cost-efficient and reliable system to collect and communicate relevant information applying savings directive. It seems more appropriate to put the burden of collecting information on the paying agent that is in most cases an intermediary that has more experience with managing information like those requested under the savings directive.
It could be very difficult to transfer the information directly from the paying agent to the competent national authority of the state of residence of the beneficial owner. Rules on the power to obtain information and for international exchange of information, between tax authorities, are a matter of national law and differ from country to country. As far as criminal law can be involved (tax evasion, money laundering…), it seems more appropriate to arrange the exchange of information system at member-states level. It is a matter of proof: this information can be relevant from a legal point of view in another member states only if the source is a EU state authority. In the Communication 16 June 2004, the Commission aimed, in general, the improvement of circulation of information between the law enforcement authorities of the Member States and the authority in charge of crime prevention. Moreover, to implement the Directive, and to help further the general aim of ensuring individuals pay the right amount of tax on cross border savings income, the competent authority of each member state has to develop a scheme to collect information about the payment of savings income and to exchange this with other countries. These scheme must be realized according to the law of each member state. Each competent authority shall produce specific guidance to assist finance industry in meeting its obligations under the Directive. This will inter alia help intermediaries decide whether they is a “paying agent” under savings directive. Maybe, it would be more effective to transfer the information directly from the paying agent to the competent national authority of the state of residence of the beneficial owner. But it seems that there are not the legal conditions for such a transfer to become possible. The exchange of relevant information from a tax law point of view, that can be also relevant from a criminal law point of view, must be managed by administrative national authorities. In conclusion, it seems not appropriate that a directive provide for a greater burden of cooperation than that generally provided by domestic tax law of each member States. I can’t understand why the directive shall impose to the paying agent, who is a private person, to act in place of national competent authority.

7) Although the directive does not mention it, does it allow the information to be transferred directly by the paying agent to the taxpayer concerned? Would your national tax law allow such a transfer?

The directive does not cover the direct transfer of information from the paying agent to the taxpayer, while article 8 establishes that “Where the beneficial owner is resident in a Member State other than that in
which the paying agent is established, the minimum amount of information to be reported by the paying agent to the competent authority of its Member State of establishment shall consist of:
(a) the identity and residence of the beneficial owner established in accordance with Article 3;
(b) the name and address of the paying agent;
(c) the account number of the beneficial owner or, where there is none, identification of the debt claim giving rise to the interest;
(d) information concerning the interest payment in accordance with paragraph 2.
Although customers do not have to be notified of their reportability nor are they required to receive copies of any reports made about them, nevertheless paying agent could (in the interests of their activities) communicate to the customers that details of their income will be transferred to the authorities under the savings directive. It seems that there is no obstacle to this kind of communication in the text of the savings directive.
As far as Italian tax law is concerned, the Decree that has implemented the savings directive, does not provide any specific provision on this matter. Nevertheless, it must be noted that there are no specific limits to such a transfer of information, provided that those information concern the beneficial owner.

8) What happens when a Member State would implement the directive, but in fact not deliver any useful information? Does the national law, or the directive provide for any mechanism of effective enforcement?

The aim of the directive is to realize effective taxation of interest payments in the beneficial owner's Member State of residence. And this aim can be achieved only through the exchange of information between Member States. If a Member State does not deliver any useful information it could bring to a violation of the aim of the directive.

The Commission should report every three years on the operation of this Directive. On the basis of this report the Commission can propose any amendments necessary to ensure effective taxation of savings income and to remove undesirable distortions of competition. Member States shall take the necessary measures to ensure the implementation of this Directive by paying agents established within their territory, irrespective of the place of establishment of the debtor of the debt claim producing the interest. Thus, if a Member State does not deliver any useful information it could bring to a breach of the aim of the directive. It is notorious that directives are binding for member States and the national authorities can only choose form and methods of
implementation. A directive is correctly implemented only if it is
effective in a member state law.
It must be cited the art. 10 of EC Treaty that establish the community
loyalty principle. This principle contains two obligations for Member
States, i.e. to cooperate loyally to facilitate the achievement of the
community’s tasks and to abstain from any measures which could
jeopardize the attainment of the community’s objectives.
The directive must be interpreted and applied in good faith. Thus the
mechanism of effective enforcement of the directive is provided by Ec
law.
The general principles of the Ec law (e.g. art. 10 EC Treaty) provide
legal basis in order to guarantee the effective enforcement of
community measures.
The effectiveness of the directive is limited by the fact that its rules
are limited to the territory of the European community.
Moreover, its effectiveness is limited by the possibility for individuals
to freely transfer money to third State. Only a global system, including
third States would be truly effective. Thus, the problem is not only the
level of information exchanged but, also, the number of states
involved.
The Italian law and the savings directive do not provide for any
mechanism of effective enforcement of directive provisions
As far as Italian tax law is concerned, it must be noted that art. 6 of
the Decree provide a pecuniary penalty if the paying agent fails to
report information to the competent authority.

9) For the definition of interest payment art. 6 of the directive qualifies
many hybrid financial instruments as the source of interest. What is in
your judgment the accuracy and the effectiveness of these criteria in
determining the amount of interest?

First of all, it is clear from the wording of art. 6 of the Directive that its
aim is to give a very broad definition of the term “interest”, with
particular reference to letter d), which says that “income realised upon
the sale, refund or redemption of shares or units in the following
undertakings and entities, if they invest directly or indirectly, via other
undertakings for collective investment or entities referred to below,
more than 40 % of their assets in debt claims as referred to in (a):
(i) an UCITS authorised in accordance with Directive 85/611/EEC,
(ii) entities which qualify for the option under Article 4(3),
(iii) undertakings for collective investment established outside the
territory referred to in Article 7.
However, Member States shall have the option of including income
mentioned under (d) in the definition of interest only to the extent that
such income corresponds to gains directly or indirectly deriving from
interest payments within the meaning of (a) and (b)”.

Given the trade off between accuracy and effectiveness, the Directive has chosen the latter, including in the definition of art. 6 of the Directive also those items of income which are not always considered to be interest. Although listing some kinds of interest, the purpose of the Community Legislator was not that of an accurate definition of what is interest and what it is not, but on the contrary, that of including the more items of income possible in art. 6, in order to prevent taxpayer from eluding the application of the disposition at issue. Moreover, para. 2 of art. 6 of the Directive states that “As regards paragraph 1(c) and (d), when a paying agent has no information concerning the proportion of the income which derives from interest payments, the total amount of the income shall be considered an interest payment”. It follows from that, that in case of doubt on the nature of an item of income, the paying agent has to consider it an interest, thus applying the disposition of the Directive.

10) What is in your view the role of the interest definition of the directive with respect to the effective taxation of such interest in the Member States? Does it impose an obligation to tax such interest?

Among the consideranda of the Savings Directive, it is stated that “Savings income in the form of interest payments from debt claims constitutes taxable income for residents of all Member States” (second considerandum)

But, as provided for in art. 1 of the Directive, “1. The ultimate aim of the Directive is to enable savings income in the form of interest payments made in one Member State to beneficial owners who are individuals resident for tax purposes in another Member State to be made subject to effective taxation in accordance with the laws of the latter Member State”.

One should assume that, in the light of these considerations, the directive is aimed at avoiding that taxes are not levied in the beneficial owner State of residence, so that double non-taxation would occur. In particular, it could be argued that, in this situation, there is in fact an infringement, or at least a distortion, of the purposes of the directive itself.

Nevertheless, it is clear that taxation in the State of residence of the beneficial owner is subject to the laws of this Member State (see art. 1, par. 1 of the Directive), i.e., the directive cannot impose any tax withdrawal which is not provided by domestic law.

For this reason, the assumption of the second considerandum has to be read as one of the funding principles of the directive that, in any case, can suffer from some exceptions, that occur when, according to the domestic law of the payee residence Member State, no tax is levied on the interest payment.

In addition to that, it has to be borne in mind the reasons that lead to the approval of the directive in object. The information exchange in
favour of the beneficial owner State is conceived to counteract the tax avoidance enacted by the taxpayer, who does not declare these items of income arising from foreign sources. If a Member State decides not to tax a particular kind of interest, this is due to economic and political reasons which cannot realize an infringement of the directive.

In general, in the context of the directive, taxation will take place in accordance with the laws of the Member State of residence of the beneficial owner, including bilateral tax treaties. The directive aims to improve effective taxation of interest in the beneficial owner State. It is understood that the State of residence of the paying agent may refrain from taxing the interest, while the State of residence of the individual beneficial owner is going to tax that item of income.

With reference to the source country (the country of the payer), art. 16 of the Directive states that a member State can levy on the interest payment other types of withholding tax than that referred to in art. 11 of the Directive for Belgium, Luxembourg and Austria, in accordance with their national laws. Thus according to the directive the State of source is free to tax the interest.

It must be underlined that the savings directive does not impose an obligation to tax interest payments.

The exception is the withholding tax on interest paid by paying agent resident in one of the three member states mentioned above, in the event that these States does not exchange any information. Thus, the savings directive is not introducing a new tax, since its aim is to ensure that EU member states have the necessary information to apply their tax law to their own residents, in respect of interest payments which they receive from any of the Member States, third countries and territories concerned.

Moreover, according to the directive, the State of residence of the beneficial owner is free to decide whether to tax or not the income.

The definition of interest payment referred to in art. 6 of the Directive is a broad one.

This Article defines the scope of the debt-claims covered by the directive and contains the so-called 'de minimis' rule. Member states have the option of excluding from the definition of 'interest payment' income from UCITS where the investment in debt-claims of such entities has not exceeded 15% of their portfolio.

It must be noted that it is not clear if member States can enlarge the interest definition implementing the directive. Member states have a number of options under which they may modify the definition of interest payment. As a result, this definition may not be the same in every member State.

Thus, one may argue that it is possible for a member state to enlarge the definition of interest payment. It must be noted that, if a member State unilaterally enlarges the definition of interest payment, that could provoke relevant problems for the exchange of information.
An interest payment could be covered by the directive in the State of residence of the paying agent while is not covered in the State of residence of the beneficial owner.

V. Questions of withholding and retention tax

1) If your country is a withholding country (Au., B., Lux., Man and the Channel Islands, Turks & Caicos for the U.K., Monaco and Andorra for F., CH. and Liechtenstein for CH. and Netherlands Antilles for NL) how are the rules for exchange of information upon request? Are there specific rules or is use made of rules on identification for foreign residents under existing tax treaties or existing national law?

According to art. 1, para. 3, of the Decree that has implemented the savings directive the paying agent shall communicate relevant information when levying the withholding tax. Art. 6 of the Decree established that the paying agent shall communicate the relevant information according to the 8 July 2005 statement implementing art. 6 of the Decree. Thus, Decree provides for specific rules for the exchange of information under the savings directive provisions (as implemented by Italian tax law).

The Italian tax administration has promulgated a ruling dealing with the communication of the relevant information (statement 8 July 2005 implementing of art. 6 of the Decree).

In particular, article 4 of the mentioned statement provide for specific technicalities to be observed by the paying agent in order to communicate the relevant information to the competent authority.

The international exchange of information could provoke constitutional and legal problem under the Italian legal system. Generally speaking, there are some legal problems because of the integration between the exchange of information system and national rules. For example, there can be legal problems with reference to the question if a document, deriving from a foreign tax authority, is valid as proof in an Italian tax procedure.

Another legal problem concerns the way in which information are taken by foreign tax authorities. Limits to the power of tax authorities, with reference to citizens fundamental freedoms, are regulated by each state by its national law and, in particular, by constitutional law. And these rules can be quite different in a foreign State.

Thus, the international exchange of information between tax authorities could provoke constitutional and legal problems. The exchange of information should take place not only under international agreement or tax directives, but also under constitutional law of each state involved. This means that the government of each state involved in the exchange of information must respect its constitutional limit.
The constitutional law of each member states can limit the use of the information exchanged. Nevertheless, European directives can realize a progressive harmonization of the rules on information relevant for tax purposes. As far as constitutional law is concerned, it must be noted that European law prevails in any conflict with domestic legislation and, because of this principle, constitutional law cannot obstacle the European law harmonization. It must be noted that the Treaty establishing a Constitution for Europe introduces an article that, for the first time, explicitly states the primacy of European law over national law. In any case, this principle was established by the European Court of Justice from the Van Gend en Loos-decision and Costa v. Enel-decision. This also means that a domestic tribunal or authority must, where possible, interpret domestic law in accordance with European law. Nevertheless, the constitutional law of each member state can limit the effectiveness of the exchange of information, by limiting the use of such information in the domestic context.

3) For the jurisdictions applying withholding tax the directive provides for a levy of “equivalent effect” on interest income referred to in art. 6 (1)(b) or (d). Has such a levy with “equivalent effect” been introduced in your country and if so how does it operate?

The Decree, that has implemented the savings directive, does not provide for a levy of “equivalent effect” on interest income as provided by art. 11, paragraph 2 (b) of the Directive.

VI. Questions of tax planning and tax avoidance

1) What is in your national tax law the relationship between your national tax system and the tax systems of your dependencies: for the U.K. the Channel Islands, Man, the crown colonies and crown dependencies, for the NL. The Netherlands Antilles, for France Andorra and Monaco, for Switzerland and Austria: Liechtenstein and for Italy San Marino? Are residents with income sourced in these countries subject to tax? Are there special rules with respect to the taxation of interest on behalf of the residents of those countries?

As far as tax relationship between Italy and San Marino is concerned, it must be noted that the two tax systems are independent. Italy has signed a double tax convention with The Republic of San Marino on 21-3-2002 but this agreement has not been yet ratified. Thus, nowadays there is no tax treaty between Italy and the Republic of San Marino for the avoidance of double taxations.
The tax relationship between Italy and The Republic of San Marino concerns mainly VAT law. The Republic of San Marino is an independent state which is part of the Customs territory of the Community [Council Regulation (EEC) No 2151/84 Article 2]. This derives from the fact that San Marino is part of the Italian customs territory. Relationships concerning the customs union between San Marino and Italy were established by the Convention of 31 March 1939. Article 44 of the Convention established the principle of the Customs Union between San Marino and Italy and article 52 of the Convention established a financial arrangement between the two republics, whereby in return for San Marino giving up certain rights (e.g. the manufacture of matches or growing of tobacco) the Republic of Italy agreed to make a lump sum annual payment to the Republic of San Marino. The rights forgone included the right to levy customs duties and similar import levies. This amount is charged to two chapters of the Italian Treasury budget.

Moreover, Under the Customs Union between Italy and San Marino all third country goods destined for San Marino are first customs cleared by Italian or other Member States customs offices. There are no transit facilities or arrangements whereby goods can cross the Community without first being put into free circulation. No duties or levies are collected by the San Marino authorities themselves. Products of San Marino origin are regarded as being in free circulation. There is a legal arrangement between the Republic of Italy and the European Community concerning the establishment and paying over of own resources to the Community involves no formula whereby the Italian authorities can make a deduction for any amounts of duty or levies attributable or paid over to San Marino. However, although no formal agreement has been made, the right of the Italian authorities to make a deduction has been accepted and approved by the Commission.

On 16 December 1991 a cooperation and customs agreement was signed between the European Economic Community and the Republic of San Marino, dealing with matters additional to trade and customs union. It must be also noted that, according to savings directive transitional provisions, the Republic of San Marino ensure effective and complete exchange of information upon request concerning payment of interest.

Generally speaking, income deriving from The Republic of San Marino and received by an Italian taxpayer is subject to tax. For example, an Italian employee who earns income from employment in the Republic of San Marino is subject to tax on that income in Italy.
Moreover, the taxes paid in San Marino can be set off against the taxes due in Italy.

The commercial relationship between Italy and the Republic of San Marino is regulated by the Decree of Ministry of Finance 24 December 1993. Specific rules are also provided for transfer of goods under the value added tax regime.

There are no special rules with respect to the taxation of interest on behalf of the residents of the Republic of San Marino.

It must be noted that The Republic of San Marino is included in the Italian black list provided by the Decree of Ministry of Finance 4 May 1999. Art. 2, para 2-bis, CAIT establish that individuals are considered Italian resident if they transfer their residence in a State included in the above mentioned black list.

As a consequence, if an Italian taxpayer transfer its fiscal residence in the Republic of San Marino he will be considered still resident in Italy, unless he proves that he is effectively resident in that State.

3) The Channel Islands, Man and the British Crown colonies and dependencies have submitted draft treaties literally incorporating the rules of the directive in these treaties? How should these treaties be interpreted if litigation arises respect to such treaties in one of those territories, in accordance with their national law, or on appeal with English law, or in accordance with the principles of E.U. law.? Quid when a litigation on such treaties occurs in a Member State? Is a E.U. law applicable and could a tribunal or court refer a preliminary question to the E.U. Court of Justice? The same question arises when litigation would occur in the Netherlands Antilles, Monaco, Liechtenstein, Andorra or San Marino or in a member State in relationship with these countries?

The Republic of San Marino signed an Agreement with the European Community providing for measures equivalent to those laid down in Council Directive 2003/48/EC on taxation of savings income in the form of interest payments. The aim of the agreement is to ensure that the Republic of San Marino adopts measures equivalent to those to be applied within the European Community to permit effective taxation of savings income in the form of interest payments. The measures involve withholding tax, a voluntary procedure for the beneficiary based on the optional supply of information to his or her tax authority in place of withholding of tax at source by the paying agent, a mechanism for information exchange on request in the event of tax fraud or equivalent offences concerning interest.

This Agreement falls under the jurisdiction of the European Court of Justice.

The Directive is intended to apply to dependent territories of EU member states. The Republic of San Marino is not a dependent territory.
5) Does the directive apply to income payments from foundations in San Marino? If not is there any equivalent local tax on such income payments?

The savings directive is into force since 1 July 2005 and agreements with certain third countries, like The Republic of San Marino for equivalent measures, are into force since that same date. According to Article 4 of the Agreement between the European Community and the Republic of San Marino, providing for measures equivalent to those laid down in savings directive, ‘paying agent’ in San Marino shall mean banks under San Marino banking law, as well as economic operators including natural and legal persons resident or established in San Marino, partnerships and permanent establishments of foreign companies. Thus, measures equivalent to those in savings directive shall be applied to income payments from foundations in San Marino.