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## Focus on: Italy CFC legislation embittered



Palazzo Chigi, Rome  
Seat of Italian  
Government

On 26 June 2009, the Italian Government adopted a legislative decree which embittered the CFC (*Controlled Foreign Company*) legislation with effect as of 1 July 2009. This decree, which should be converted into law by the Parliament within 60 days in order to remain into force, aims at combating tax havens according to the recent OECD directives.

The amendments regard one of the two conditions provided forth in order to obtain the non-applicability of the anti-avoidance rule at hand through tax ruling. The taxpayer resident in Italy should, in fact, demonstrate that the Controlled Foreign Company carries on an effective business activity in the market of the State or of the territory where it is established. Such a requirement is considered not to be met whether more than 50% of the income of the cfc derives from the management, detention or investment of securities, claims or other financial activities, from payments of royalties or intra-group services.

In addition, the Italian CFC legislation, as amended, applies with reference to countries not included in the black list whether the following two conditions are met:

1. The CFC is subject to an effective tax in its country which is 50% lower than Italian tax (i.e. 13,75%);
2. More than 50% of the income of the cfc derives from the management, detention or investment of securities, claims or other financial activities, from payments of royalties or intra-group services.

Such a provision does not apply whether the Italian taxpayer demonstrates that the investment abroad does not represent an artificial mechanism aimed at obtaining an undue tax advantage.

### USA

## IRS issues industry directive regarding dividend deduction and transfer pricing adjustments

The US Internal Revenue Service (IRS) issued a directive which provides guidance to IRS field auditors for cases that involve both a dividend repatriation issue and a transfer pricing adjustment. Where a US parent corporation is undercompensated by its controlled foreign company (cfc), Internal Revenue Code (IRC) requires a primary upward allocation of income (conforming adjustment) to the US parent and a downward correlative allocation to the cfc. The revenue procedure allows this required repatriation of additional cash from the cfc to the parent, mandated as a conforming adjustment, to be established as an account payable owed by the cfc to the parent and not as taxable income.

In 2004 a new Section was added to the US Internal Revenue Code in order to permit a 1-year window for US corporations to repatriate earnings from cfc's at a reduced rate of US tax by means of an 85% dividends received deduction (DRD). The amount of the dividend must be reduced for purposes of the DRD to the extent it was deemed to have been funded directly or indirectly by the US parent. This is achieved by comparing the related party indebtedness (RPI) owed or deemed to be owed by the cfc to related parties on two measurement dates. The issue in this directive is the timing of the creation of the account payable for purposes of its inclusion in measuring RPI.

The Directive concludes that these accounts payable are includable in RPI and are deemed to be established on the last day of the tax year for which the transfer pricing adjustment is made. The Directive includes sections on Examination Guidance to field examiners on this issue, and Guidance for Closing Cases with the specific procedures to be followed. Additionally, the Directive contains three examples demonstrating the impact of adjustments on the RPI balance.

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**NETHERLANDS****New economic stimulus package**

On 4 June 2009, the Lower House adopted the economic stimulus package, which will enter into force as of 1 July 2009 and will introduce the following tax measures:

- Application of energy savings deduction to energy savings in rented dwellings. Contrary to what earlier was intended, this measure will apply from 1 June 2009 and not from 1 April 2009. The budgetary savings from this postponement will be used to subsidize double glazing;
- A reduction of the corporate income tax rate in the second tax bracket (i.e. for profits between EUR 40,000 and EUR 200,000) for small and medium-sized companies to 20% for the years 2009 and 2010; currently, the rate is 23.5%;
- An increase of the penalty for non-declaration of savings and investment income (Box 3 income) to a maximum of 300% of the additional tax due;
- Restriction of the tax amnesty, which implies that no penalty is imposed on the additional tax levied, to 2 years after the filing of the tax return in which the income had not yet been reported.

**GIBRALTAR****Details of budget for 2009-2010**

As of 1 July 2009, the main measures of the Budget for 2009-2010 will enter into force. Measures regarding corporate taxation are summarised as follows:

- Corporate tax rate, set at 27% for 2008-2009, will drop to 22% for 2009-2010 and will be 10% with effect from 1 January 2011.
- with effect from 2009-10 until 31 December 2010, a 10% start up rate applies for companies established after 1 July 2009. Such companies will be charged to tax on an actual year basis. In prescribed circumstances, these provisions may also apply to businesses commenced after 1 July 2007;
- the preceding year basis of taxation will be replaced by an actual year basis, and the basis rules on the commencement of a business will be abolished
- the benefits provided to exempt companies currently holding exemption certificates will not be withdrawn until midnight on 31 December 2010.
- With reference to taxation of individuals, the Budget introduces the following amendments:
- two new tax bands (0% and 10%) are introduced under the Gross Income Based (GIB) system, whose current intermediate rate is reduced to 29% from 30%;
- all allowances under the Allowances Based System (ABS) are increased by 2.8%;
- carry back of contributions for retirement annuity contracts and personal pension schemes is abolished;
- for high net worth individuals and Category 2 individuals, the minimum tax liability is increased to GBP 20,000 (from GBP 18,000). The maximum amount of income on which they must pay tax is increased to GBP 70,000 (from GBP 60,000).

**INTERNATIONAL MODELS****The corporate taxation in Malta**

After having joined the European Union, Malta represents a very interesting jurisdiction for investment. Maltese corporate tax rate is established at 35%. However, shareholders enjoy low effective rates of Maltese tax as Malta's full imputation system of taxation allows generous unilateral relief and tax refunds on the distribution of profits. Shareholders can in fact apply for a tax refund of 6/7ths of the tax paid by the company on those trading profits that have been used to pay a dividend. This results in an effective Maltese tax rate of 5% on trading income.

Where corporate profits are derived from interest and royalties, the tax refund to the shareholder is 5/7ths of the tax paid by the Maltese company, which results in an effective Maltese tax rate of 10% on passive income. Where the Maltese company has obtained double taxation relief on the foreign passive income, the tax refund to the shareholder is 2/3rds of the tax paid by the Maltese company.

Malta provides for a Participating Holding Exemption regime, according to which dividends and capital gains derived from a participating holding in a non-resident company are exempt from income tax.

In order to benefit from the regime at hand, the shareholding of the Maltese company in the foreign company must satisfy at least one of the following conditions:

- The holding is 10% or more of the equity capital of the foreign company or
- The holding is a substantial equity investment of at least €1,164,000 and the holding is held for an uninterrupted period of at least 183 days or
- The Maltese company:
  - o Holds at least 1 equity share and has an option over the balance or
  - o Holds at least 1 equity share and has power to appoint a director

Income of foreign sources which has been subject to a foreign withholding tax can benefit from a tax credit, which should not exceed the total tax liability in Malta. To that purpose, taxpayer may rely either on the great number of double tax conventions signed by Malta or on domestic provisions establishing a unilateral tax relief.



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