

Transfer of Residence and Exit Taxation in EU Law: the Italian Approach

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1. Introduction

The present configuration of the Italian income tax system is characterized by two important features, with reference to the EU freedom of establishment.

On the one hand, the transfer of residence abroad by a company or enterprise is expressly considered as a gain, in terms of the exit tax pursuant to Art.166, Tuir.

On the other hand, the transfer of residence abroad is specifically regulated by anti-avoidance and anti-evasion provisions. In particular, there is a presumption of residence in Italy on the part of companies formally resident abroad, but maintaining a "substantial" presence in the Italian territory. This presumption was recently introduced, together with the power of tax authorities to consider such transfers of residence invalid.

In this connection, the overall picture would appear to give rise to serious problems in connection with the principle of non-discrimination and the freedom of establishment. In fact, the transfer of residence abroad on the part of entrepreneurs, collectives or individuals gives rise to a tax liability. Moreover, a transfer of this kind, especially in the case of companies, may mean that the taxpayer is required to prove that the transfer is genuine or that residence abroad is not an avoidance strategy. However, an analysis of the compatibility of the national tax system with EU freedoms must take other fundamental elements into account.

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Firstly, the ECJ has declared the incompatibility of the exit tax with the freedom of establishment, basing its ruling on conditions which seem non-existent in the Italian system. The cases examined by the ECJ concerned the transfer of residence by individuals. National provisions for entrepreneurs were not deemed to be applicable. In these entrepreneurial cases, the Italian tax system does not currently apply an exit tax, which is limited to individuals engaging in business activity².

Secondly, in order to determine the impact of national rules on freedom of establishment, it is essential to take criteria used to value assets in the country where the residence is transferred into account. Based on the variable combination of criteria of "exit" taxation and appraisal rules of "entry" assets, completely different fiscal consequences can ensue. One such consequence is double taxation.

Finally, it is necessary to emphasize that companies and, generally speaking, entities other than individuals are set up under a national legal system and they exist solely on the basis of national legislation³. This

² In par. 2.3 the issue of exit taxation for workers will be discussed.

³ European Court of Justice, case C-81/87, 27/9/1988, *Daily Mail*, in *Racc.*, 1988, 5483. Similar conclusions can be drawn in relation to the definition laid down in the law regulating companies, in the field of international private law. The European Court of Justice has ruled that the freedom of establishment gives rise to the right of undertakings established in one Member State to operate in other Member States, applying the law of the State where they are incorporated, which means the State where their registered office is located. In cases in which the main office of the undertaking is transferred to another State, that State is not only required to recognise the undertaking set up in the State of incorporation, but may not apply regulations that are more restrictive than those laid down by the legislation of the State of incorporation. See ECJ 9 March 1999, C-212/97 Centros; ECJ 5 November 2002, C-208/00 Überseering; ECJ 30 September 2003, C-167/01 Inspire Art; BALLARINO, *Sulla mobilità delle società nella comunità europea*, in *Riv.soc.*, 2003, 669 ss.; LOMBARDO, *La libertà comunitaria di stabilimento delle società dopo il "caso Überseering" tra armonizzazione e concorrenza fra ordinamenti*, in *Banca,borsa,tit.cred.*, 2003, 457 ss.; WYMEERSCH, *Il trasferimento della sede della società nel diritto societario europeo*, in *Riv.soc.*, 2003, 723 ss.; CONTALDI, *Il diritto comunitario delle società tra evoluzioni giurisprudenziali e legge di riforma della materia*, in *Dir.un.eur.*, 2003, 711 ss.; BENEDETTELLI, *"Mercato" comunitario delle regole e riforma del diritto societario italiano*, in *Riv.soc.*, 2003, 699 ss. BALLARINO, *Sulla mobilità delle società nella comunità europea*, in *Riv.soc.*, 2003, 669 ss.; LOMBARDO, *La libertà comunitaria di stabilimento delle società dopo il "caso Überseering" tra armonizzazione e concorrenza fra ordinamenti*, in *Banca,borsa,tit.cred.*, 2003, 457 ss.; WYMEERSCH, *Il trasferimento della sede della società nel diritto societario europeo*, in *Riv.soc.*, 2003, 723 ss.; CONTALDI, *Il diritto comunitario delle società tra evoluzioni giurisprudenziali e legge di riforma della materia*, in *Dir.un.eur.*, 2003, 711 ss.; BENEDETTELLI, *"Mercato" comunitario delle regole e riforma del diritto societario italiano*, in *Riv.soc.*, 2003, 699 ss.

means that the choice of the connection criteria, and the means of assessment of the real nature of the criteria are decided by national lawmakers.

The present study aims at exploring the factors involved in the way national fiscal systems are structured. The Italian system appears to adopt a different paradigm compared to the general European provisions on the limitations on the freedom of establishment.

2. The transfer of individual residence

2.1. The absence of an exit tax for subjects who are not entrepreneurs

The Italian fiscal system does not impose a specific exit tax in the case of the transfer of residence by individuals not engaging in business activities. The characteristic features of the cases examined by the ECJ in the *de Lasteyrie du Saillant*⁴ and *N*⁵ decisions do not appear to exist in Italian law⁶.

Clearly, in the above-mentioned decisions, the Court asserted that national provisions that deem a transfer of residence to be equivalent to the realisation of unrealised gains from the sale of shares are incompatible with EC law. The restrictive effect on the freedom of establishment could be attributed to the discrimination resulting from the difference of regime between subjects transferring their fiscal residence (with consequent tax liability only in relation to accrued and not effectively realised capital gains)

⁴ See ECJ 11 March 2004, C-9/02 *de Lasteyrie du Saillant*.

⁵ See ECJ 7 September 2006, C-470/04 *N*.

⁶ See LUPI, *Coerenza del sistema fiscale tra dividendi esteri ed exit tax*, in *Dialoghi dir. trib.*, 2004, 1365.

and other subjects (for whom on the other hand single taxation in the case of "monetisation" of unrealised gains was provided)⁷.

In Italy the Unified Body of Laws dealing with income tax, specifically concerning the taxation of capital gains, provides that capital gains are taken into consideration in terms of income as *sundry profits* (art. 67 par.1 lett. c, c-bis, Tuir) only as the result of a sale of assets. The only important fact is receipt of this income⁸.

The transfer of residence abroad does not appear to result in the taxation of unrealised gains in Italy, nor of those accrued in the period of possession coinciding with fiscal residence in Italy. Such gains will not be subject to taxation in Italy even in the future.

In cases where a subject from abroad has transferred his/her residence to Italy and sells assets that were held in the period of non-Italian residence (or in more general terms, during the period of application of the Italian law), it should be noted that this capital gain is then taxed in its entirety in Italy⁹.

As a result, it is generally correct to argue that a subject who relocates his/her residence abroad can achieve the effect of avoiding Italian taxation

⁷ See DE PIETRO, *Compatibilità comunitaria di exit tax su partecipazioni rilevanti*, in *Rass.trib.*, 2006, 1377 ss.; KOTANIDIS, *Case Hughes de Lasteyrie du Saillant: French Exit Tax Incompatible with the Freedom of Establishment.*; RICCI, *Exit taxes tra diritto di cittadinanza e libertà di stabilimento: il caso Hughes De Lasteyrie Du Saillant*, in *Riv.dir.fin.sc.fin.*, 2004, II, 95 ss.

⁸ There are significant differences, with regard to the time of calculation of capital gains, between systems of "managed savings" and "savings under administration". See MARCHETTI, *Il risparmio nel sistema delle imposte sui redditi*, Milano, 1997, 71 ss.; LUPI, *Diritto tributario, Parte Speciale*, Milan, 2007, 185 ss.; MIGNARRI, *Profili inerenti alla tassazione delle plusvalenze finanziarie per i soggetti residenti*, in *Il fisco*, 2008, 4469 ss.

⁹ In relation to various incomes, it is not possible to identify just one norm (as is the case with Art. 166 Tuir) capable of giving rise to a "structural" requirement to link tax liability only to capital gains accrued during the period of application of the Italian tax system. In this connection see Studio del Consiglio Nazionale del Notariato, *Profili fiscali ai fini dell'imposizione diretta del trasferimento in Italia della sede di una società estera*, est. PURI, 18/7/2008, forthcoming in *Studi e Materiali*, 2008, note no. 7. It is also possible for specific norms of international tax law to be applied which adopt different evaluation criteria for shareholdings, for the purpose of taxing capital gains, in order to avoid double taxation, as provided in Art. 13 of the Agreement on double taxation between Italy and Germany, discussed in RIS. AG. ENTRATE n. 67/E, 30/3/2007. See Studio del Consiglio Nazionale del Notariato, *Profili fiscali ai fini dell'imposizione diretta del trasferimento in Italia della sede di una società estera*, est. PURI, del 18/7/2008, forthcoming in *Studi e Materiali*, 2008, note no. 7.

on capital gains accrued but not still realised¹⁰; however, it is necessary to specify that, as the criterion of worldwide profit for a subject who is no longer resident does not apply, these capital gains could be subject to Italian taxation based on the "source of income" criterion.

Art. 23 par.1 lett. f), Tuir, provides for taxation of non-residents for "capital gains deriving from the sale of shares in resident companies "¹¹.

Moreover, this article shows consideration for the various assets and/or economic activities of the transferred subject, in order to determine whether, with reference to the different categories of income, the tax liability continues to apply in Italy.¹²

2.2. The exit tax provided for individual entrepreneurs

There is a need also to examine the case of natural persons who conduct business activities. Individual entrepreneurs are subject to the exit tax provided by Art.166 Tuir: the transfer of residence gives rise to the taxation of assets that are not owned by a permanent establishment in Italian territory. Postponing a fuller discussion on the way the norm operates, it is necessary here only to emphasize that Art.166, paragraph 1, Tuir, provides for separate taxation for unrealised gains by individuals acting as entrepreneurs and by partnerships (Art. 17, par.1 lett. g, l).

2.3. The question of exit taxation for self-employed workers

A more complex issue is that of natural persons who are self-employed. As a result of amendments to Art. the 54, Tuir, by DI n. 223 dated 4/7/2006¹³ and by the Finance Act 2007¹⁴, the increase (but not the decrease)¹⁵ in the

¹⁰ See LUPI, *Coerenza del sistema fiscale*, cit., 1365.

¹¹ Excluding the cases considered in Art. 23, (1), f), nn.1,2,3.

¹² Regarding source criterion see FRANSONI, *La territorialità nel diritto tributario*, Milan, 2004, 369 ss.

¹³ Implemented by Law 248 dated 4/8/2006.

¹⁴ Law 27/12/2006, no. 296.

¹⁵ As a result of the amendment introduced by Law no. 296/2006.

value of assets instrumental to the professional activity¹⁶ is deemed to contribute to income. According to the law, the cases in which there is a realization of unrealized gains are those that, in the entrepreneurial income regime, are capable of generating revenue or an increase/decrease in the value of company assets: sales, compensation, personal or household consumption, and the allocation of assets for purposes other than business use.¹⁷

Partially anticipating matters to be discussed later, the case of the transfer of residence abroad can also be considered as the “allocation of assets for purposes other than business purposes” (as mentioned above) and, in certain circumstances, could result in avoidance of taxation in Italy on instrumental assets.

Furthermore, self-employed persons are subject to an exit tax, which depends on the application of a general rule and not on a specific provision. This brief analysis shows the specific provisions relating to Italian exit tax; it provides an overview of the principles regulating the taxation of enterprise income, rather than dealing with specific cases, to be analysed in more detail below.

A significant differentiation between individual entrepreneurs and self-employed persons is to be seen in cases where, despite the transfer of residence abroad, the Italian tax regime remains applicable due to the source of income criterion. Pursuant to Art.23 Tuir, taxation in Italy of profits “deriving from activities exercised in the Italian territory” applies to self-employed persons, whereas in the case of entrepreneurs, it applies only in cases in which they have a permanent establishment in Italian territory.

¹⁶ With an exception for works of art, antiques and collections.

¹⁷ See Studio del Consiglio nazionale del Notariato, *Redditi di lavoro autonomo: novità relative ai criteri di determinazione introdotte dalla “manovra finanziaria 2007”, est.FORTE*, approvato dalla Commissione Studi Tributari il 2/3/2007; Circolare Consiglio Nazionale Dottori Commercialisti e degli esperti contabili, n. 1/IR del 12/5/2008, *Il nuovo regime fiscale degli immobili strumentali per l'esercizio di arti e professioni*, in *Il fisco*, 2008, 3887 ss. SACCHETTO, *I redditi di lavoro autonomo: nozione e disciplina tributaria*, Milan, 1984, *passim*.

As a result, the Italian fiscal regime does not apply to instrumental assets in cases in which a person who has moved abroad ceases to engage in a regulated professional activity in Italy or, even though it takes place, if he/she avoids making use (totally or partially) of instrumental assets utilised before the transfer of these assets abroad.

2.4. The transfer of residence to tax havens

The evaluation of the impact of the Italian fiscal regime on freedom of establishment of individuals must take into consideration Art.2 par. 2bis, Tuir, as this rule provides for a *juris tantum* presumption of residence in Italy for nationals who remove their names from municipal registers and move to countries other than those on the white list to be issued by a Decree of the Ministry of Finance¹⁸.

As a result of this white list, the above-mentioned presumption should apply to the transfer of residence of individuals to countries considered tax havens that do not provide an adequate exchange of information¹⁹.

In cases in which this rule is applicable to EU Member States²⁰, there may be a problem of compatibility with the fundamental freedoms of the Treaty. There might be some restriction²¹ given that these provisions may have a

¹⁸ The reference to a "white list" was introduced by Law no. 244, 24/12/2007 (finance law 2008), that came into force on 1/1/2008, that provided that up till the previous tax year the measures in force until 31/12/2007 were to apply; these measures made reference to countries and territories with a privileged tax regime listed in the black list in D.M. 4/5/1999. See MARINI, *I nuovi confini dei paradisi fiscali*, in *Rass.trib.*, 2008, 637 ss. In this connection reference may be made to MELIS, *Riflessioni intorno alla presunzione di residenza fiscale di cui all'art. 10 della l. 23 dicembre 1998, n. 448*, in *Rass.trib.*, 1999, 1077 ss.; MAISTO, *La residenza fiscale delle persone fisiche emigrate in Stati o territori aventi regime fiscale privilegiato*, in *Riv.dir.trib.*, 1999, IV, 51 ss.

¹⁹ See Marini op.cit.

²⁰ Also with regard to the black list at present in force, that applies to EU Member States such as Cyprus and Malta. As regards the limits placed on individual countries in relation to States that have signed the Agreement on the European Economic Area, see ECJ 26 October 2006, C-345/05 Commission v Portugal; ECJ 18 January 2007, C-104/06, Commission v Sweden.

²¹ The European Court of Justice makes a distinction between direct discrimination (European Court of Justice, case C-270/83, 27/1/1986, *Avoir fiscal*, in *Raccolta*, 1986, 302; ID., case C-1/93, 12/4/1994, *Halliburton*, in *Raccolta*, 1994, 1156.), indirect discrimination (European Court of Justice, case C-330/91, 13/7/1993, *Commerzbank*, in *Dir.prat.trib.*, 1994, II, 439 ss.) and restrictions (ECJ 12 February 1974, C-152/73 Giovanni Maria Sotgiu v Deutsche

dissuasive effect on persons resident in Italy planning to move to another Member State, thus exercising the general freedom of movement and residence (Art.18 ECT)²² or, in the case of undertakings²³, the freedom of establishment (Art.43 ECT)²⁴.

However, this rule appears to be compatible with the fundamental freedoms of the Treaty.

This opinion is not based on the procedural nature of this provision that binds the taxpayer to provide evidence of the actual place of residence. The procedure is not a sufficient element to consider this provision legitimate pursuant to EU law, as it leads to a different treatment among taxpayers. The ECJ has on several occasions affirmed, also in relation to VAT, that violations of rights safeguarded by EU law have to be evaluated in practical terms, considering the effects produced by national provisions on taxpayers²⁵.

Thus, the procedural nature of this rule is not relevant, but its aim and the way it works are. On the one hand, the aim is important as the intent of

Bundespost). See AMATUCCI, *Il principio di non discriminazione fiscale*, Padua, 1998, 117 ss.; ADONNINO, *Il principio di non discriminazione nei rapporti tributari fra Paesi membri secondo le norme della CEE e la giurisprudenza della Corte di Giustizia delle Comunità*, in *Riv.dir.fin.sc.fin.*, 1993, I, 63 ss.; DI PIETRO (ed.), *Libertà economiche e divieto di discriminazione nell'imposizione diretta*, Padua, 2004, *passim.*; SACCHETTO, *Armonizzazione fiscale nella Comunità Europea*, in *Enc.giur.it.*, Rome, 1988, II; PISTONE, *La non discriminazione anche nel settore dell'imposizione diretta: intervento della Corte di Giustizia*, in *Dir.prat.trib.*, 1995, I, 1471 ss.

²² See ECJ 29 April 2004, C-224/02 Pusa; ECJ 20 September 2001 C-184/99, C-184/99 Grzelczyk; Opinion of the Advocate General, 30 March 2006, C-470/04 N.

²³ The exercise of an economic activity is at the basis of Art.43 of the Treaty. In relation to the possibility of characterising the situation of someone who owns shares in a company, the ECJ has repeatedly stated the principle that "*Where a Community national lives in one Member State and has a shareholding in the capital of a company established in another Member State which gives him substantial influence over the company's decisions and allows him to determine its activities, as is always the case where he holds 100% of the shares, that may thus fall within the freedom of establishment*" (ECJ 7 September 2006, C-470/04 N); ECJ 13 April 2000, C-251/98, Baars, p.22; ECJ 21 November 2002, C-436/00 X and Y, p.37; ECJ 12 September 2006, C-196/04 Cadbury Schweppes, p.31.

²⁴ The freedom of establishment protected by the Treaty is both primary and secondary. See MELIS, *Libertà di circolazione dei lavoratori, libertà di stabilimento e principio di non discriminazione nell'imposizione diretta: note sistematiche sulla giurisprudenza della Corte di Giustizia delle Comunità Europee*, in *Rass.trib.*, 2000, 1151 ss.

²⁵ See MONDINI, *La nuova responsabilità solidale del cessionario Iva e la sua compatibilità con il diritto comunitario*, in *Rass.trib.*, 2005, 755; RODRÍGUEZ IGLESIAS, *Sui limiti dell'autonomia procedimentale e processuale degli Stati membri nell'applicazione del diritto comunitario*, in *Riv.it.dir.pubbl.com.*, 2001, 5 ss.

dealing with abusive phenomena is considered by the ECJ a general interest imperative capable of justifying the violation of fundamental freedoms²⁶, particularly in the case of fraudulent residence statements²⁷. On the other hand, the way this provision is implemented is relevant because the above-mentioned objective has to be achieved in compliance with the principle of proportionality²⁸. The presumption is relative, not absolute; there is no limit to contrasting evidence that may be provided by taxpayers; there are no problems of retroactivity preventing the exercise of the right to prove a genuine transfer of residence in practical terms. In other words, the provision is designed in such a way as to ascertain whether the transfer of residence abroad is genuine or not, in the light of objective situations such as the transfer of residence to tax havens, giving rise to the need to adopt measures to protect the national financial interest.

3. The transfer of residence of companies and entities operating under private law

3.1. The transfer of the registered office as an amendment of the company's statute: fiscal consequences of continuity of the entity

The fiscal effects of the transfer of residence of companies and, in general, of entities must necessarily start from an analysis of the transfer. This is due to the position of companies, either partnerships or commercial companies, in the Italian tax system. According to Art. 6 par. 3 and Art. 81 Tuir, commercial companies are considered to generate exclusively business

²⁶ See ECJ 12 May 1998, C-367/96, Kefalas; ECJ 16 July 1998, C-264/96, Imperial Chemical Industries.

²⁷ See ECJ 13 December 2005, C-446/03, Marks&Spencer.

²⁸ See GALETTA, Il principio di proporzionalità nella giurisprudenza comunitaria, in Riv.it.dir.pubbl.com., 1993, 837 ss.; MELONCELLI, Il controllo di proporzionalità e la giurisprudenza comunitaria in materia fiscale, in Riv.dir.trib., 2005, I, 806 ss. ECJ 31 March 1993, C-19/92, Kraus/Land Baden-Wuttemberg; ECJ 30 November 1995, C-55/94, Gebhard/Consiglio dell'Ordine degli Avvocati e Procuratori di Milano; ECJ C-415/93, Bosman et al; ECJ 15 May 1997, C-250/95, Futura Participations e Singer.

income²⁹. As already mentioned³⁰, commercial contracts represent the area of application of the tax regime for undertakings so that all the factors relating to the effectiveness and validity of this contract affect the tax regime. It is therefore important to highlight the fact that the taxation of undertakings is closely linked to continuity of the entity involved: as long as an undertaking exists, it will be taxed on the basis of the tax regime for undertakings³¹. On the contrary, if the transfer of the registered office abroad were to be considered as a winding up or liquidation of the company, this would mean the non application of the tax regime for undertakings. Nonetheless, the prevailing interpretation in commercial law is that the transfer of the registered office abroad is a modification of the company incorporation³², and the same may be said of demergers and transformations³³.

As a result, the company does not disappear or initiate a winding-up procedure simply by moving its registered office abroad. The same conclusion may be reached also considering other criteria which, pursuant to Art.73 par.3, Tuir, establish the residence of the undertaking in Italy and,

²⁹ Commercial firms can generate only company income. For entities, on the other hand, the commercial nature of the activity is related to the business purpose, either exclusive or principal, and not to the type of entity, as is the case for undertakings. Having clarified this point, the observations relating to commercial companies also apply to commercial entities. Non-commercial entities, in the same way as natural persons, can only generate other types of income. See TASSANI, *Autonomia statutaria delle società di capitali e imposizione sul reddito*, Milan, 2007, 63 ss.

³⁰ See TASSANI, *cit.*, 55 ss.

³¹ It may also be the case that, after the winding up of the undertaking, the former partners continue to carry on the business on either a collective or an individual basis. In the event that there is continuity in economic terms, there is also continuity in legal terms, unless there has been a transformation (in a legal sense) of the undertaking. From the point of view of taxation, a case of this kind will be deemed to be the winding up of one undertaking and the establishment of another. With regard to these aspects and the consequences in terms of the invalidity or ineffectiveness of the company contract in relation to the application of company tax regulations, see TASSANI, *op. cit.*, 97 ss.

³² The Italian Civil Code considers this to be a case giving rise to the right to withdraw for SpA (Art.2437 c.c.) and Srl (Art.2473 c.c.) shareholders.

³³ See FIMMANO', *Trasferimento della sede sociale all'estero e principio di incorporazione*, in *Le società*, 1997, I, 574; SANTUS, *In tema di trasferimento della sede all'estero ed omologazione parziale*, in *Nuova giur.civ.comm.*, 1996, I, 857; BALLARINO, *La società per azioni nella disciplina internazionaleprivatistica*, in AA.VV. , *Trattato delle società per azioni*, diretto da Colombo e Portale, Torino, IX, 1994, pag. 66 ss.; SANTA MARIA, *Spunti di riflessione sulla nuova norma di diritto internazionale privato in materia di società ed altri enti* in *Riv. Soc.*, 1996, pag. 1102.

therefore, the “transfer” abroad of the registered office and the main activity. The continuity of the entity, not affected by the transfer of residence abroad, should not therefore give rise to tax liability on unrealised gains at the time of transfer and recognition of fiscal values; however, this conclusion appears to be incorrect for two reasons. Firstly, even though it is true that a transfer of residence abroad does not result in the winding up of the entity involved, it cannot give rise to an exemption of company assets from the tax regime for undertakings only because the Italian fiscal regime no longer applies. Secondly, because the continuity of fiscal values is not conditioned by provisions of the tax system where the undertaking was previously resident, but rather by provisions of the tax system in the country to which the undertaking has been transferred.

3.2. The transfer of residence abroad as the realization of gains: the exit tax provided by Art. 166 Tuir

The transfer of residence abroad does not automatically result in the liquidation or winding-up of a company, but may nevertheless exclude company assets from the tax regime for undertakings. With regard to the transfer of a company abroad³⁴, the *personal* connection with Italian territory is missing and as a result business activity may no longer be relevant in fiscal terms³⁵. In other words, although the legal person still

³⁴ The transfer of residence usually takes place by means of the relocation of the registered office abroad. However, if, in spite of the modification of the by-laws, the place of management and the main business are not relocated abroad, the undertaking will continue to be considered resident in Italy pursuant to Art. 83 (3) Tuir. Another case to be considered is that of “double or triple residence” of the undertaking and the methods laid down by international agreements and national provisions for avoiding double (or triple) taxation. See FANTOZZI-VOGEL, voce *Doppia imposizione-internazionale*, in *Digesto disc.priv sez comm*, Turin, 1990, V, 181; MARINO, *La residenza*, cit., 209 ss.; VAN RAAD, *Dual Residence and the 1977 Model Treaty Artiche 4(1)*, in *Eu.Tax.*, 1990, 27 ss.; VAN GENNEP, *Dual Resident Companies*, in *Eu.Tax.*, 1991, 141 ss.

³⁵ Also in the case of other “extraordinary” changes to company by-laws, the continuous existence of the subject may give rise to tax liability, due to the effect of the removal of assets from the company tax regime, as in the case of the transformation of an undertaking into another type of entity. See TASSANI, cit., 129 ss.

exists, the transfer to another country may preclude the application of Italian tax provisions.

This will certainly be the case in all those instances where the connection criterion of residence is not replaced by the criterion of the source, leading to permanent establishment. Accordingly, the presence of a permanent establishment may be a sufficient requirement to apply the entrepreneurial tax regime³⁶ to the business carried out in Italy through the permanent establishment, and to impose taxes on the assets of the permanent establishment. The most significant aspect is that, in the Italian company tax system, where enterprise assets are utilised for a purpose other than for the company's main business purpose, then they are treated as capable of generating profits or unrealised losses/profits³⁷ that are no longer within the scope of the company's main business purpose. This provision, considered to be a standard rule³⁸, applies to all business income generated either by individual entrepreneurs or companies³⁹. In the light of the above analysis, it is possible to state that the exit tax in Art.166 Tuir⁴⁰ expresses a principle relating to business income. Under this provision, the transfer abroad of residence by individual entrepreneurs or companies engaged in business activities results in a realisation, at book value, of company assets, unless these assets remain within a permanent establishment in the Italian

³⁶ See FANTOZZI-MANGANELLI, *Qualificazione e determinazione dei redditi prodotti da imprese estere in Italia*, in *Studi in onore di V. Uckmar*, Padua, 1997, 413; GARBARINO, *Forza di attrazione della stabile organizzazione e trattamento isolato dei redditi*, in *Rass.trib.*, 1990, I, 427; PERRONE, *La stabile organizzazione*, in *Rass.trib.*, 2004, 794 ss. DELLA VALLE, *La nozione di stabile organizzazione nel nuovo Tuir*, in *Rass.trib.*, 2004, 1597 ss.; FRANSONI, *La determinazione del reddito delle stabili organizzazioni*, in *Rass.trib.*, 2005, 73 ss.; LOVISOLO, *La stabile organizzazione nel nuovo modello OCSE*, in *Corr.trib.*, 2006, 109 ss.

³⁷ Artt.85, codicil 2, and 86, codicil 1, lett.c) Tuir.

³⁸ See FALSITTA, *La tassazione delle plusvalenze e sopravvenienze nelle imposte sui redditi*, Padua, 1978, 95; MICCINESI, *Le plusvalenze d'impresa, Inquadramento teorico e profili ricostruttivi*, Milan, 1993, 158. For another interpretation of the case in which assets are transferred to a use other than the original business purpose, see NUSSI, *Trasferimento della sede e mutamento della residenza "fiscale": spunti in tema di stabile organizzazione e regime dei beni d'impresa*, in *Rass.trib.*, 1996, 1351 ss. TASSANI, cit., 216 ss.

³⁹ As noted above, the assignment of assets to purposes other than the original business purpose also applies, on the basis of the present formulation of Art. 53-bis Tuir, in the case of freelance workers, with reference to assets that are instrumental to their occupation or profession.

⁴⁰ See ZIZZO, *Il trasferimento della sede all'estero*, in SACCHETTO & ALEMANNI (eds.), *Materiali di diritto tributario internazionale*, Milan, 2002, 210 ss.

territory. Moreover, this provision clearly links the taxation of unrealised enterprise gains to the continuity of application of the fiscal regime for businesses. As a result it provides that the unrealised gains of the permanent establishment abroad are considered to be realised, since, after the transfer of residence abroad, there is no way to provide for any kind of continuity. The element that determines taxation is the removal of the business from application of the fiscal regime for business due to the loss of fiscal residence, whereas in order to avoid such a consequence it is sufficient to set up a permanent establishment in Italy to which the assets of the enterprise can be assigned. In the latter case it will only be possible to avoid taxation of assets that are assigned to the permanent establishment and only as long as these assets remain with the permanent establishment. Art.166 Tuir gives rise to a tax liability on these assets if they are transferred from the permanent establishment in Italy. Additionally, Art. 166 Tuir currently in force (as modified by D.lgs 199/2007⁴¹), includes specific rules for the calculation of losses prior to the transfer of fiscal residence⁴², and in addition it provides that the transfer of residence of a company does not automatically result in tax liability for shareholders⁴³.

3.3. Analysis of the Italian exit tax in the light of ECJ's jurisprudence: no restriction on the freedom of establishment

The evaluation of the compatibility of the exit tax (Art.166 Tuir) with EU law must take into consideration the role played by Art.166 Tuir in the company tax regime. From the discussion so far, it is evident that this provision is not

⁴¹ Implementing Directive 2005/19/CE.

⁴² It is laid down in Art. 166, (2-*bis*) that losses incurred in the tax period prior to the period in which the cross-border transfer of the tax residence takes place, not offset by income generated in that period, may be deducted from income generated by the undertaking pursuant to Art. 84, Tuir, and on the conditions and limits laid down by Art. 181, Tuir.

⁴³ With regard to the provisions concerning the transfer of company's registered office abroad, D.lgs 199/2007 does not simply transpose the Directive, but extends the measures laid down in the Directive to the transfer of SEs and SCEs.

a derogation from the principles of the system, but an application of general tax provisions in cases in which a company's assets are used for purposes other than⁴⁴ the main business purpose of the company. This includes all cases in which the business tax regime no longer applies. As a result, the taxation of unrealized business earnings becomes relevant at a systematic level for the following two reasons. Firstly, because tax liability traditionally relates to income earned by the owner of an asset, with the sale of the asset and its conversion into another form of wealth⁴⁵. Secondly, because consumption and use by the individual or the individual's family of enterprise assets for purposes other than the company's main business purpose give rise to realization, even though no payment is made⁴⁶. According to the two cited ECJ cases regarding the exit tax, in order to ascertain whether Member State regulations are compatible with EU law or not, the fundamental point is the dissuasive effect of exit taxes on the freedom of establishment, due to the different treatment between nationals remaining in the country and those leaving it. In the examined decisions, the restriction of fundamental freedom was closely connected to the derogatory treatment that applied to nationals moving abroad. Specifically, discrimination arose from tax liability on unrealized gains, whereas normally⁴⁷ taxation should coincide with the moment of realization. It is

⁴⁴ A systemic role of this kind is highlighted, also with regard to the loss of residence arising from cross-border mergers, by MICCINESI, *Le plusvalenze d'impresa*, cit., 240; LUPI, *Profili tributari della fusione di società*, Padua, 1988, 60 ss.; ZIZZO, *Le riorganizzazioni societarie nelle imposte sui redditi*, Milan, 1996, 343 ss.; SILVESTRI, *Il regime tributario delle operazioni di riorganizzazione transnazionale in ambito Cee*, in *Riv.dir.fin.sc.fin.*, 192, 456; PORCARO, *Trasferimento di sede all'estero* in LUPI & STEVANATO (eds.), *La fiscalità delle operazioni straordinarie d'impresa*, Milan, 2002, 732; MARINO, *Profili fiscali delle riorganizzazioni di imprese con elementi di ultraterritorialità*, in *Dir.prat.trib.*, 1993, 2110; MARINI, *Trasferimento di sede all'estero e rilevanza della "stabile organizzazione" ai fini della titolarità di reddito d'impresa*, in *Dialoghi dir.trib.*, 2005, 89 ss.

⁴⁵ See MICCINESI, cit., 196; the sale or transfer of assets includes those transfers for which payment is made in the form of assets, exchange, assignment and compensation. In addition, in the opinion of the present author, the sale or transfer of assets should also include the transfer of assets to business partners. TASSANI, *op.ult.cit.*, 221; FANTOZZI, *Contributo allo studio della realizzazione dell'avviamento quale presupposto dell'imposta di ricchezza mobile*, in *Riv.dir.fin.sc.fin.*, 1964, I, 33 ss.; ID., *Ancora in tema di realizzazione delle plusvalenze*, in *Riv.dir.fin.sc.fin.*, 1965, I, 457 ss.

⁴⁶ See FALSITTA, cit., 46.

⁴⁷ See ECJ 7 September 2006, C-470/04, N "In this case, analogously with what the Court has already found in relation to a similar system, a taxpayer wishing to transfer his residence

therefore possible to affirm that such discrimination does not exist in the Italian system on the basis of Art.166 Tuir. This provision was introduced not solely in relation to the transfer of residence abroad, as it embodies a general principle applicable to all persons in every case where there is objectively no application of the business tax regime⁴⁸, even though there is no transfer of residence. Accordingly, wherever an entrepreneur terminates the entrepreneurial activity without realizing all the assets, or a company is transformed into a non-commercial entity, the entrepreneur or company are taxed on unrealized gains, since their assets are to be assigned to a purpose other than the original purpose; the same conditions apply to assets of entities moving abroad if they do not assign these assets to a permanent establishment in Italy.

It is the opinion of the author that the declarations of the European Commission, which consider principles laid down in ECJ judgments applicable to companies⁴⁹, have to be considered in a critical light as this interpretation gives rise to difficulties relating to the rationale and the operation of the Italian exit tax. It is therefore not possible to attribute to this provision any direct or indirect discrimination on grounds of nationality, nor any specific discriminatory treatment for those who decide to transfer their residence abroad. Consequently, no restriction on the freedom of establishment⁵⁰ seems to be present.

outside Netherlands territory, in exercise of the rights guaranteed to him by Article 43 EC, was subjected at the time of the facts to disadvantageous treatment in comparison with a person who maintained his residence in the Netherlands. That taxpayer became liable, simply by reason of such a transfer, to tax on income which had not yet been realised and which he therefore did not have, whereas, if he had remained in the Netherlands, increases in value would have become taxable only when, and to the extent that, they were actually realised. That difference in treatment was likely to discourage the person concerned from transferring his residence outside the Netherlands".

⁴⁸ See ROMANO, *Sull'illegittimità delle imposizioni fiscali connesse al trasferimento di residenza all'interno dell'Unione Europea*, in *Rass.trib.*, 2004, 1291; FICARI, *Trasferimento della sede all'estero, continuità della destinazione imprenditoriale e contrarietà al trattato CE dell'"exit tax" sulle plusvalenze. latenti*, in *Rass.trib.*, 2004, 2146 ss.

⁴⁹ See Communication n.825 19/12/2006

⁵⁰ For a recent analysis of the principle of non-discrimination and the concept of restriction according to ECJ case law see ROSSI-MACCANICO, *Principi comunitari di fiscalità diretta delle imprese. Il principio di non discriminazione*, in *Fiscalità internazionale*, 2008, 226 ss. On the subject, NUZZO, *Libertà di stabilimento e perdite fiscali: il caso Imperial Chemical Industries (ICI) plc*, in *Rass.trib.*, 1999, 1814 ss.

However, it would not be correct to affirm the existence of a restriction on fundamental freedoms only on the basis of a general dissuasive effect due to taxation in the State of origin. In other words, it would mean that a violation of EU freedom takes place because the person moving abroad would gain a greater advantage by deferring or avoiding taxation rather than incurring a tax liability at the time of the transfer. This construction of the concept of restriction would substantially devalue and excessively simplify it, as the dissuasive effect of the restriction may appear to be always present in every form of tax liability, as the concept of tax liability is normally not attractive to taxpayers. It is obvious that this approach would be mistaken, as the ECJ is clear in linking the concept of restriction to the concept of discrimination: as explained by Advocate General Maduro in the *Marks & Spencer* case, it is “a matter of pursuing discrimination against Community nationals wishing to assert their rights derived from the freedom of movement”⁵¹.

3.4. Art. 166 Tuir and the justification of the “coherence of the tax system”

The conclusion reached by the author so far is that Art. 166 Tuir is compatible with EU law as there is no discriminatory/restrictive effect on the freedom of establishment. However, it may be said that, even though Art. 166 Tuir was regarded as incompatible with the freedom of establishment on the basis of a broad definition of restriction, the above-mentioned incompatibility could be justified, relying on ECJ case law, on the grounds of “coherence of the tax system”⁵².

As already argued by distinguished authors, the justification of “coherence of tax system” is noteworthy as taxation based on Art. 166 Tuir originates

⁵¹ See Opinion of the Advocate General, p.28, C-446/03, *Marks&Spencer*.

⁵² See ECJ 11 March 2004, C-9/02 de Lasteyrie du Saillant; ECJ 7 September 2006, C-470/04 N.

from “a structural systematic requirement⁵³”, not from anti-avoidance or anti-evasion purposes. Moreover, the imposition of a tax liability when the company tax regime ceases to be applied is a response to the need for a provision allowing the taxation of assets on the grounds of deductions relating to these assets from which taxpayers have previously benefited⁵⁴.

Finally, the solution protects national jurisdictions on the basis of the principle of territoriality as recently explained by ECJ judgments⁵⁵; according to the principle of territoriality, taxation can be considered to be balanced and proportional. This fiscal effect represents the consequence of a general imposition that does not exist in the cases decided by the ECJ judgments concerning exit taxation⁵⁶.

3.5. Directive 1990/434 and taxation of transfer of residence

The conclusion that the exit tax in Art.166 Tuir is not incompatible with the freedom of establishment since it is not restrictive, and justified in term of the coherence of the fiscal system, can be further supported by an analysis of the fiscal model in Directive 1990/434 dated 23/07/90⁵⁷, later amended by Directive 2005/19 dated 17/2/2005⁵⁸.

⁵³ See LUPI, *Coerenza del sistema*, cit., 1366; MARINI, *Trasferimento di sede all'estero e rilevanza della “stabile organizzazione” ai fini della titolarità di reddito di impresa*, in *Dialoghi dir.trib.*, 2005, 95

⁵⁴ See PIZZONI, *La compatibilità delle exit tax con il diritto comunitario*, in *Riv.dir.trib.*, 2004, III, 51; MICCINESI, cit., 158.

⁵⁵ See ECJ 18 July 2007, C-231/05, Oy AA; ECJ 7 September 2006, C-470/04, N; DE PIETRO, *op.ult.cit.*

⁵⁶ For this reason, in *de Lasteyrie du Saillant* and *N* the ECJ declared national measures to be disproportionate, even though they were intended to safeguard the principle of territoriality. In the latter case, the Court ruled on the “proportionality” of the requirement that a declaration be submitted at the time of transfer (see DE PIETRO, *op.cit.*). It is worth repeating that such a conclusion is appropriate in relation to income deriving from the sale or transfer of assets held by physical persons, in relation to which the general rule is that the tax liability arises from the actual transfer of the assets. In relation to company income, for which there is a general tax provision that does not depend on the actual transfer of assets, with the transferred assets no longer coming under the tax regime for companies, taxation at the time of the transfer appears to be proportionate, in application of the principle concerning the need for a coherent system.

⁵⁷ Implemented by Law n.225, 20/08/1990.

⁵⁸ Implemented by Dlgs.n.119, 6/11/2007.

It is well known that Directive 1990/434 provides for a system of taxation applicable to cross-border restructuring operations (mergers, divisions, transfers of assets, exchange of shares concerning companies of different Member States) aiming at neutrality⁵⁹ in terms of tax liability. Mergers⁶⁰ appear to be particularly interesting as they offer various analogies to the transfer of companies abroad. According to national provisions and to this Directive, in the case of a merger or transfer abroad, the entity does not disappear as the merger or the transfer is not regarded in fiscal terms as a case of realization. However, a cross-border merger or transfer may result in the loss of the "personal" connection of the company to the country and consequently in the exclusion of his assets from the Italian business tax regime. In these cases, illustrious authors⁶¹ have described cross-border mergers as the realization of enterprise assets for different purposes, in terms of Italian tax law. In cases in which the assets of a merged Italian company are not assigned to a permanent establishment in Italy (owned by the non-resident company resulting from the merger), there will be a tax liability on unrealized gains arising from enterprise assets that have been transferred out of the entrepreneurial regime. Clearly, this case is analogous to the one in Art.166 Tuir, the only difference being that the loss of the Italian tax residence depends in the first case on the cross-border merger, whereas in the second case it depends on the company's decision to move abroad⁶². Furthermore, the fiscal consequences laid down by Directive 90/434 are compatible with the rationale on which Art.166 is

⁵⁹ See CARINCI, *Le riorganizzazioni societarie e le imposte sui redditi*, in AA.VV., *Lo stato della fiscalità dell'Unione Europea*, coordinato da DI PIETRO, Roma, 2003, II, 510 ss. On the general matter, also see SILVESTRI, *Il regime tributario delle operazioni di riorganizzazione transnazionale in ambito CEE*, in *Riv.dir.trib.*, 1996, I, 428 ss.

⁶⁰ Similar considerations apply in the case of a demerger. For a discussion of the analogy between mergers and demergers, in the perspective of Directive 90/434, see SILVESTRI, *op.ult.cit.*, 641 ss.

⁶¹ See SILVESTRI, *cit.*, 476. On this point, see also ZIZZO, *Le riorganizzazioni societarie nelle imposte sui redditi*, *cit.*, 342 ss.

⁶² Clearly it is also possible to imagine the case of an undertaking whose registered office is located outside Italy, but is deemed to be resident in Italy because its administrative offices and/or principal business are located in Italian territory. In this case, the transfer of residence will be the result not of the change of the registered offices of the undertaking, but by the decision to relocate the administrative offices and/or principal business. It is evident that in the case of double or triple residence, problems of multiple taxation can arise.

based. A cross-border merger gives rise to the loss of fiscal residence in the State of origin of the merged company; in addition, if the company's assets are not assigned to a permanent establishment in that country, then they are regarded as being used up for different purposes and, according to Directive 90/434, subject to taxation on the basis of their unrealised gains. However, this is not in contrast with the principle of neutrality⁶³. In conclusion, taxation of a company's assets that are transferred out of the fiscal regime due to the loss of fiscal residence (without the monetization of unrealised gains) is considered by Directive 90/434 to be compatible with a general EU taxation model⁶⁴.

3.6. Directive 2005/19 and the transfer of the registered office of European Companies and European Cooperative Societies

Directive 2005/19 amended Directive 90/434, adding section IV-ter which includes "Rules applicable to the transfer of the registered office of an SE or an SCE". These provisions aim to guarantee the fiscal neutrality of the transfer of the registered office of European companies and European cooperative societies, not giving rise to any tax liability in the EU State of origin provided that a permanent establishment is set up there and the assets of the transferred company are assigned to this permanent establishment (Art.10-ter Directive 90/434).

This rule is similar to that of Art.166 Tuir. Additionally, Dlgs. 199 dated 6/11/2007 modified Art.166 Tuir by applying provisions therein not only to the transfer of the registered office of an SE and SCE, but to all cases of the transfer of the fiscal residence of companies and enterprises. Thus, Art.166

⁶³ See CARINCI, *op.ult.cit.*, 511. Under the terms of the Directive, other elements are also considered important, to safeguard neutrality, including that of the continuity of assets subject to tax liability and the adoption of a "notional tax credit". This is not the appropriate setting to carry out an in-depth discussion of the Directive under examination. It must be pointed out, however, that both these matters will be considered below, with specific reference to the transfer of residence to another country.

⁶⁴ See MELIS, *Profili sistematici*, cit., 59; FICARI, *Reddito di impresa e programma imprenditoriale*, Padova, 2004, 157-8.

Tuir is compatible with Directive 2005/19. This compatibility appears to be important as it offers evidence that the tax liability model based on taxation of the transferred assets of the company not assigned to a permanent establishment in the State of origin is compatible with the fundamental freedom of establishment. It would be difficult to conclude otherwise, considering the choice of this model of tax liability in Directive 2005/19 that, aiming at fiscal neutrality, regulates the transfer of registered offices for SEs and SCEs⁶⁵. Furthermore, the requirement of a uniform interpretation of EU law precludes any other conclusion and, according to ECJ case law⁶⁶, provides further evidence that there is no problem of infringement of the freedom of establishment for those national provisions that comply with a tax liability model sanctioned by EU Law.

3.7. Outbound taxation and recognition of fiscal values in the inbound state

The analysis will now focus on the relationship between the taxation of outbound assets and the recognition of inbound fiscal values in case of transfer of residence abroad. It is possible to imagine that a company leaves a State in which tax is calculated on current values in order to move to another State which values its assets at historic cost. In this case there would be negative consequences for taxpayers as they could deduct lower amortization rates and, in case of the realization of assets, would be taxed on gains accrued in the State of origin and thus already taxed there.

On the other hand, it is possible to imagine a company that gives up its fiscal residence in one State without being subject to an exit tax and whose assets, in the inbound State, are estimated at current value. In this case there would be no taxation since the unrealized gains accrued in the State of origin would be taxed neither at the time of transfer, nor at a later

⁶⁵ See ROMANO, *op.ult.cit.*

⁶⁶ About the uniform application of EC Law see ECJ 27 November 2003, C-407/01, Zita Modes; ECJ 27 February 2003, C-373/00, Adolf Truley; ECJ 9 November 2000, C-357/98, Yadam; ECJ 19 September 2000, C-287/98, Linster and Others.

date⁶⁷. Both these consequences appear to be detrimental in terms of the EU rationale of market freedoms⁶⁸. Nonetheless, although the combination of the fiscal policies of the two States may give rise to negative and dissuasive effects for taxpayers who decides to transfer their residence, it does not seem to lead to the conclusion that the different national provisions are incompatible with the fundamental freedom of establishment. It is a coordination problem between the national tax systems concerning direct tax liability rather than a matter of compliance of these individual systems with the freedoms in the Treaty.

Once national provisions are found to be compatible with EU law, (as, according to this author's analysis, in the case of Art. 166 Tuir) solutions to problems relating to a company's transfer of residence arising from a combined application of different States' provisions have to be found by means of harmonization of the dissimilar tax systems⁶⁹. This harmonization should be achieved by means of a legislative process rather than by relying on the interpretation of the ECJ. The Commission⁷⁰ is aware of this problem and in order to solve it has developed prospective solutions that have not yet been implemented⁷¹. In term of harmonization it is a serious issue considering that Directive 19/2005 has provided regulations for the transfer of residence of the SE and SCE, but has omitted to provide rules aimed at avoiding the risk of double taxation relating to the transfer of residence.

⁶⁷ Problem highlighted by the European Commission, see Communication n.825 19/12/2006.

⁶⁸ See Communication n.825 19/12/2006; MELIS, *Profili sistematici*, cit., 40 ss.

⁶⁹ See SACCHETTO, *Armonizzazione fiscale nella Comunità Europea*, cit.

⁷⁰ See Communication n.825 19/12/2006.

⁷¹ See Proposal for a Council Directive 17/10/2003, COM(2003)613, which made provision for a notional tax credit on capital gains relating to permanent establishments located in other Member States; MIELE, *In via di recepimento la direttiva su operazioni straordinarie transfrontaliere*, in *Corr.trib.*, 2007, 2751.

3.8. Permanent establishment abroad and the notional tax credit provided by Dlgs 199/2007

The aim of avoiding double taxation, at least in certain cases, has led the Italian legislator, with the enactment of D.lgs. 199/2007, to apply the notional tax credit to the transfer of residence within the EU.

In cases in which (after a merger, demerger or transfer of assets) the transferring company has a permanent establishment located in another Member State, Art.10, par.2 of Directive 90/434 provides that the State of origin of the transferring company has the right to tax unrealized gains relating to the permanent establishment, on condition that a deduction is granted equal to the tax that the State where the permanent establishment is located would have required if it had not had to apply the Directive.

The Directive prevents the State of permanent establishment from taxing unrealized gains at the time of the extraordinary operation and, by granting a notional tax credit, it is possible to avoid a harmful effect on the taxpayer as well as double taxation of unrealized gains relating to transferred assets⁷².

The current Art.179 par.3 Tuir, as amended by Dlgs.199/2007, provides the notional tax credit applied to the transfer of an Italian company with a permanent establishment abroad, but within the EU. The “virtual” taxation of the permanent establishment abroad is calculated with reference to the open market value that the other Member State would have ascertained in the case of realization at open market value of the above-mentioned permanent establishment. The EU⁷³ rationale of this provision is manifest, in that it aims at avoiding the double taxation which would result from either the Italian exit tax on unrealized gains relating to the permanent establishment, or the value attributed in the other Member State to the

⁷² See SILVESTRI, cit., 488-9; LUPI, *Primi appunti in tema di fusioni, scissioni e conferimenti “transnazionali”*, in *Boll.trib.*, 1992, 1302.

⁷³ See Proposal for a Council Directive 17/10/2003, COM(2003)613 . As already noted, the extension of notional tax credits is not required by the current formulation of Directive 90/434/CE.

assets of the permanent establishment, that would necessarily be the historic value⁷⁴.

At the current stage of development of EU and national legislation, the risk of double taxation survives in all those cases where this provision does not apply, as double taxation is likely to arise from a combination of different national regimes.

3.9. Evaluation criteria of assets allocated in Italy by transfer of residence from abroad

In order to conclude this analysis, it is important to ascertain which regime is applicable in case a company or enterprise moves its residence to Italy; the main issue is the recognition of the fiscal value of the assets, that are subject to the business tax regime⁷⁵.

The Tuir makes no specific provision and therefore it is essential to rely on the general principles regulating business tax. In the literature it has been argued that inbound assets are taxed at normal value as described in Art. 9 par.3 and 4 Tuir⁷⁶. So far, there could be taxation on unrealised gains accrued during the time of residence in Italy as the connection between "accrued income" and tax sovereignty would be sufficient to justify taxation in Italy⁷⁷.

⁷⁴ See MIELE, cit., 2751 ss.

⁷⁵ The question does not appear to arise in the case of an undertaking resident in a country other than Italy but with a permanent establishment in Italy which transfers its residence for tax purposes to Italy, at least with regard to assets that were already assigned to the permanent establishment. These assets continue to be subject to the Italian tax regime and as a result continue to be considered at their 'historic' value. In cases of an undertaking with assets in a country other than Italy, the problem arises as to how to assess these assets for the Italian tax system.

⁷⁶ See GALLIO-FURLAN-STEVANATO-LUPI, *Trasferimento della residenza, exit tax e valorizzazione dei beni nell'ordinamento di arrivo*, in *Dialoghi dir.trib.*, 2007, 575 ss.; DE CAPITANI DI VIMERCATAE, *Brevi note in tema di trasferimento della residenza ed entrata di beni nella sfera impositiva italiana*, in *Dir.prat.trib.*, 2008, II, 36 ss.; CANCELLIERE, *La valorizzazione fiscale dei beni esteri immessi nel territorio nazionale*, in *Fiscalità internazionale*, 2007, 392 ss.

⁷⁷ See LUPI, *Trasferimento della residenza, exit tax e valorizzazione dei beni nell'ordinamento di arrivo*, in *Dialoghi dir.trib.*, 2007, 582; FURLIAN, *Il trasferimento della sede (e della residenza fiscale) in Italia di società di diritto comunitario: profili civilistici*,

Art.166 Tuir and in general taxation relating to the use of company assets for purposes other than company activity appear to be based on this principle. As recently noted in an authoritative study,⁷⁸ "there is no reason why the State making a claim to tax the entrepreneur's unrealized gains accrued during the period of residence in the Italian territory, even though realized only after the transfer, should be able to consider taxable unrealized gains accrued elsewhere, but realized later". However, it is important to highlight the fact that the interpretation by Italian tax authorities, as stated in resolutions 67/E dated 30/03/2007 and 345/E dated 5/8/2008, is partially discordant with the solution proposed by the present author. According to the Italian tax authorities, both criteria, historic cost and current value, may theoretically be used to determine the fiscal value of assets transferred to Italy pursuant to a transfer of residence. The current value criterion appears to be the most suitable in cases where the foreign state applies an exit tax, whereas the historic cost criterion is to be preferred where the transfer takes place without any taxation of unrealized gains. In the recent resolution 345/2008, Italian tax authorities have based their interpretation on the principle of continuity, considering the current value criterion as appropriate only in the case of legal and fiscal discontinuity. This approach, according to the present author, is open to criticism as it confuses two different matters: *legal continuity* of the subject and *realization* in fiscal terms.

The legal continuity of a company moving its registered office⁷⁹ does not require, under private law, dissolution and re-establishment of the

contabili e fiscali, in *Il fisco*, 2007, 3264 ss.; CANCELLIERE, *La valorizzazione fiscale dei beni esteri immessi nel territorio nazionale*, in *Fiscalità internazionale*, 2007, 399.

⁷⁸ See Studio del Consiglio Nazionale del Notariato, *Profili fiscali ai fini dell'imposizione diretta del trasferimento in Italia della sede di una società estera*, est. PURI, dated 18/7/2008, forthcoming in *Studi e Materiali*, 2008.

⁷⁹ As rightly noted by tax authorities in Resolution n.9/E dated 17/1/2007, for the purposes of Art.25, L.218 dated 31/1/95, it is necessary for the transfer of the registered office to comply with the provisions of the State of origin as well as the State to which the transfer is made. For this reason, legal continuity, as recognised by the Italian system, applies only when the transfer of the registered office abroad, without consequences such as winding-up/liquidation, is recognised by the legal system also in the State of origin. See MELIS, *Profili sistematici*, cit., 27; SANTA MARIA, *Società (dir.internaz.)*, in *Enc.Diritto*, XLII, Milan, 1990,

company; there is no need for liquidation to take place. From a fiscal point of view, the mere transfer of the registered office does not result in a realization of the company's assets. Moreover, the connection between the time of residence abroad and time of residence in Italy has to be taken into consideration for several different purposes⁸⁰.

Legal continuity does not prevent the effects of realization on company assets from taking place where the tax system of the state of origin of the company moving to Italy has a provision similar to Art.166 Tuir. In these circumstances, the transfer of residence will take place with *legal continuity effects*, but will give rise to a tax liability.

Additionally, it does not seem appropriate to carry out a tax evaluation of inbound assets on the basis of the taxation of assets in the State of origin, as in this case the national tax criteria would depend on the fiscal preferences of another State. The solution proposed by Italian tax authorities appears to be inspired by a need for pragmatism and fairness in terms of overall taxpayer evaluation. Italian tax authorities aim at avoiding double taxation when opting for the evaluation of assets at current value in the case of exit taxation levied by the State of origin, whereas the choice of the historic value criterion in the absence of exit taxation in the State of origin is aimed at preventing inadvertent non-taxation. However, there is no legal framework supporting this interpretation as the TUIR allows taxation only of unrealized gains accrued as from the moment when assets start to

898; ID., *Le società nel diritto internazionale privato*, Milan, 1970, 106; CAPOTORTI, *Il trasferimento di sede di una società da uno Stato all'altro*, in *Foro it.*, 1958, IV, 209 ss.

⁸⁰ See RIS. AG.ENTRATE, n. 9/E del 17/1/2007 takes the legal continuity of the undertaking transferred to Italy as the basis for the continuity of the "period of taxation", stating that the entity will be deemed to be resident in Italy for the entire tax period if the transfer of the registered office is completed before the expiry of a period consisting of a number of days that is less than half of the tax period. Otherwise, the transferred company is deemed by Italian tax authorities to have been set up ex novo, thus starting a new tax period, and the company would be considered to be immediately resident in Italy, in the same way as a newly established undertaking. The RIS. AG. ENTRATE n. 345/E dated 5/8/2008, again on the basis of the principle of legal continuity, provides that the requirement of the period of possession for the application of PEX (Art. 87, Tuir) is to be verified by taking into account the possession relating to the period in which the undertaking transferred to Italy had been resident in a country other than Italy. GALLIO, *Il trasferimento della residenza fiscale in Italia secondo l'Agenzia delle Entrate: alcuni dubbi*, in *Il fisco*, 2006, 1022 ss.; RIGHINI, *Trasferimento della sede e mutamento della residenza fiscale in corso d'anno: l'interpretazione dell'Agenzia delle Entrate*, in *Il fisco*, 2006, 1950 ss.

incur tax liability in Italy. Moreover, the choice of different evaluation criterion on the basis of the tax regime in the State of origin of the subject moving to Italy may result in a different treatment of this subject and give rise to a strong risk of discrimination and violation of the fundamental freedom of establishment. Finally, the choice by the State of origin to exempt outbound unrealized gains from taxation is a merely internal decision that may result in tax privileges.

3.10. Residence presumptions in Italy of companies and entities and the “tax avoiding” transfer of residence abroad by companies

In recent years, in Italy several provisions aimed at thwarting simulated and/or tax avoiding residence abroad have been adopted. To start with, it is essential to consider the residence presumptions in Italy of IRES subjects provided in Art. 73 Tuir.

The D.l. 223/2006 (implemented by L. 248/2006) added to Art. 53 Tuir two paragraphs (5-bis and 5-ter) regarding companies and entities controlling (according to Art.2359, par.1, c.c.) companies and commercial entities resident in Italy. The place of effective management of these controlling subjects is deemed to be Italy, unless otherwise demonstrated, on either of the two following conditions: controlling companies and entities must be controlled, either directly or indirectly, by subjects resident in the Italian territory or the majority of their board members must be resident in Italy⁸¹. Recently, D.l. 25/6/2008 n.112 (entering into force on 5 August 2008) added to Art.73 Tuir a further paragraph (5-quater) according to which residence of companies and entities is deemed to be in Italy if “the majority of their capital is invested in real estate closed-end fund shares” (according to Art. 37, D.lgs. 58/98) and “if they are controlled directly or indirectly, through a trust company or an intermediary, by subjects resident in Italy”.

⁸¹ See MELIS, *La residenza fiscale dei soggetti Ires e l'inversione dell'onere probatorio di cui all'art. 73, commi 5-bis e 5-ter, Tuir*, in *Dir.prat.trib.int.*, n.3, 2007.

It is not the aim of the present author to conduct a detailed analysis of these provisions, however they appear to share common inspiration as both confer more extensive investigative powers to tax authorities, placing the burden of proof on the taxpayer in all circumstances where there is evidence of a permanent connection with the Italian territory of subjects that are foreigners only in formal terms. Accordingly, these provisions endeavour to achieve manifest evidence of connection criteria (registered office, place of effective management, main object of activity) provided in Art.73, par.3, Tuir and so far, considering also what has already been said⁸², they do not appear to be incompatible with the EU freedom of establishment⁸³.

On the contrary, Art.1 D.lgs n.199 dated 6/11/2007 - that amended the "general⁸⁴" anti-avoidance provision in Art. 37 bis, e), DPR 600/73 – may raise a problem of compliance with EU law.

Since 1/1/2008, when this provision became effective, tax authorities have been entitled to consider *tax avoiding*, for the purposes of this same provision, the transfer of a company's fiscal residence abroad.

An illustrious author⁸⁵ has declared that the scope of this provision should be limited, as it should not apply in the case of a newly founded company abroad and the simulation of residence abroad (already regulated by Art.73

⁸² See paragraph 2.4.

⁸³ In this sense, it is necessary that no limitations are made to the taxpayer's opportunity to provide counter evidence, and in addition the object of the proof has not to be changed. In the cases in clauses 5bis and 5 ter, they may provide evidence that the place of management is abroad, despite other substantial elements locating activity in Italy. The provisions mentioned above do not affect the legal criteria for attributing residence in Italy, e.g. introducing new criteria, but simply modify the burden of proof on taxpayers during the procedure. Any discordant interpretation would be deemed to be irrational at Constitutional level and disproportionate at EU level. See DE MITA, *Principi di diritto tributario*, Milan, 2007, 89 ss.; TOSI, *Le predeterminazioni normative nell'imposizione reddituale*, Milan, 1999, 93 ss.; CIPOLLA, *La prova tra procedimento e processo tributario*, Padua, 2005, 657 ss.; TOSI, *Le predeterminazioni normative nell'imposizione reddituale*, Milan, 1999, 93 ss). Sul tema, MARINO, MARZANO, LUPI, *La residenza delle società e controllo tra schemi OCSE ed episodi giurisprudenziali interni*, in *Dialoghi dir.trib.*, 2008, 91 ss.; SERINO-PARPIGLIA, *La sede dell'amministrazione nell'attribuzione di residenza fiscale delle persone giuridiche: criticità operative*, in *Il fisco*, 2008, 4297 ss.

⁸⁴ See FANTOZZI, *Il diritto tributario*, Turin, 2003, 164.

⁸⁵ See MICCINESI, *Elusione e trasferimento all'estero della sede della società: la montagna ha partorito il topolino*, in *Giur.trib.*, 2008, 97.

Tuir) and, taking into consideration Art.166 Tuir, attempts to avoid unrealized gains taxation.

In particular, this would apply in all cases in which a company transfers its registered office abroad, without at the same time moving its productive activity⁸⁶ or other "substantial" connections with Italian territory (e.g. real estate, shares, residence of controlling shareholders, etc.). These substantial elements would, within the meaning of the new Art.37 bis, Dpr 600/73, have the function of implementing a real transfer of residence, resulting in tax benefits, deemed to be invalid by tax authorities.

Even though it will be necessary to wait for rulings on these cases in order to evaluate the real impact of the new provision, it is appropriate to highlight the prospective contrast of this provision with the freedom of establishment. The ECJ has stated in various decisions that the freedom of establishment includes the right by which companies can choose the Member State which applies the most favourable legal provisions, also in fiscal terms, for the location of their registered office⁸⁷. Member States are entitled to adopt any appropriate measure to avoid abuses, but have to limit the application of these provisions to cases of fraud and simulation relating to the company structure deriving from artificial arrangements⁸⁸.

Nevertheless, in cases when a company really transfers its residence to another Member State, locating its place of effective management abroad, there is neither fraud nor simulation as both the structure of the company and the residence abroad are real⁸⁹. Thus, the possible finding that such a

⁸⁶ See MICCINESI, *op.ult.cit.*, 98.

⁸⁷ The ECJ 9 March 1999, C-212/97, Centros; ECJ 5 November 2002, C-208/00, Uberseering; ECJ 30 September 2003, C-167/01, Inspire Art; ECJ 12 September 2006, C-196/04, Cadbury Schweppes, applying the freedom of establishment principle with regard to income tax, has recently ruled that the fact that "a Community national, whether a natural or a legal person, sought to profit from tax advantages in force in a Member State other than his State of residence cannot in itself deprive him of the right to rely on the provisions of the Treaty"; analogously, see ECJ 11 December 2003, C-364/01, Barbier p.71; BEGHIN, *La sentenza Cadbury-Schweppes e il "malleabile" principio della libertà di stabilimento*, in *Rass. trib.*, 2007, 983 ss.

⁸⁸ See MICCINESI, *cit.*, 98.

⁸⁹ See ECJ 12 September 2006, C-196/04, Cadbury Schweppes "a national measure restricting freedom of establishment may be justified where it specifically relates to wholly artificial arrangements aimed at circumventing the application of the legislation of the

transfer of residence is void as determined by tax authorities does not seem to be compatible, in these cases, with EU Law⁹⁰.

4. Conclusions

The full implementation of the freedom of establishment and the removal of fiscal barriers precluding the transfer of residence are objectives that are difficult to achieve as they depend on many different but closely related factors.

It is not only a matter of exit taxes provided by national systems on income accrued but not realized and relating to the choice of moving residence abroad. In order to safeguard the fiscal neutrality of business/economic operations, the taxation/non taxation of outbound assets must be related to the recognition and evaluation of inbound assets adopted by the State to which the transfer is made. Both these aspects must be taken into consideration as a matter of symmetry when evaluating the impact of the provisions of a Member State on the freedom of establishment.

From the point of view of the needs either of the system as a whole or of the national laws, it is necessary to guarantee a balanced partition of individual States' powers to levy taxes not only in order to safeguard national financial interests, but also to avoid double taxation (or inadvertent non-taxation) and therefore to avoid risks in terms of freedom of establishment.

In the perspective of an "ideal" tax system, there are various solutions that take into consideration the variety of factors involved; some suggestions

Member State concerned". It follows that, in order for a restriction on the freedom of establishment to be justified on the ground of prevention of abusive practices, the specific objective of such a restriction must be to prevent conduct involving the creation of wholly artificial arrangements which do not reflect economic reality, with a view to escaping the tax normally due on the profits generated by activities carried out on national territory"; ECJ 12 December 2002, C-324/00, Lankhorst-Hohorst, p.37; ECJ 13 December 2005, C-446/03, Marks & Spencer, p.57.

⁹⁰ On the incompatibility of this provision with principle of freedom of establishment, see MICCINESI, cit., 98.

were made in the Communication of the European Commission dated 2006. Nonetheless, EU law is not at this time able to provide a harmonized system of rules regulating the fiscal treatment of the transfer of residence within the EU, as the instruments offered by EU law – Freedom of establishment and movement, Directive 90/434, and the specific provisions for the transfer of SE and SCE registered offices – allow only partial approaches.

It is not only a matter of the lack of direct tax harmonization or the fragmentation of secondary legislation, but rather of ascertaining precisely how EU law affects and limits national legislators, considering that the lack of harmonization and consequently of a common approach will leave most of the related problems unsettled. In this sense, the analysis of Italian fiscal law appears to be paradigmatic.

To start with, this analysis has shown that Art.43 of the EC Treaty is not, by itself, a sufficient instrument to guarantee the full realization of freedom of establishment.

This statement will no longer appear to be paradoxical if it is considered that the evaluation of the compatibility/incompatibility of national fiscal systems, within the meaning of Art.43, is not able to take into consideration effects of connections between outbound and inbound Member State legal systems. So far, the Italian legal system appears to be compatible with Art. 43 EC Treaty, even with regard to procedural rules providing presumptions regarding residence in Italy. However, there might be a significant EU compatibility problem concerning the recent rule that considers the transfer of residence by a company to be potentially tax avoiding, even though it mainly depends on future case law interpretations. According to the principles laid down by the ECJ, in *de Lasteyrie du Saillant* and *N*, it is possible to note that the Italian system does not provide an exit tax for individuals (nor in the case of shareholdings owned by individuals moving their residence) and that outbound taxation provided in Art.166 Tuir for companies and entrepreneurs (including implicit taxation of self-employed persons) does not appear to be restrictive/discriminatory and, in any case, is justified by the requirements of “coherence of the tax system”.

Nevertheless, as already explained, the effects of double taxation, as well as inadvertent non-taxation, may arise from the variable connections with other national laws, either when Italy is the inbound or outbound state; these effects are extremely detrimental to the effectiveness of the freedom of establishment. These consequences cannot be precluded only by Art.43 of the EC Treaty and secondary EU rules would be needed. In the perspective of harmonization, the fact that the EU legislator has provided effective solutions neither when the transfer of residence involves an SE or SCE (Directive 2005/19) nor in other cases, appears to be a serious issue.

In the absence of a systematic approach at Community level, the development of the Italian system in terms of provisions and interpretation has shown the need for such an approach, if not the autonomous search for national solutions.

Accordingly, the D.lgs 199/2007 extends the notional tax credit to the transfer of residence of companies within the EU, an instrument capable of avoiding double taxation on permanent establishments abroad.

Also the administrative interpretation concerning the evaluation of enterprise assets "moved" to the Italian system by means of a transfer of residence is based on the idea of a global approach, that makes it possible to take into consideration, either in the state of origin or in the state of arrival, the entire fiscal treatment of the subject. According to the present author, this interpretation is to be criticized as lacking appropriate legal support. However, it correctly demonstrates the need, due to the aims of competitiveness and coherence of national systems, for the implementation of values on which a common market and, especially, a common system is based.