NEW RULES ON FOREIGN TRUSTS WITH GREY AREAS

The new tax regime, introduced by Article 13 of Law Decree no. 124 of 26 October 2019, concerning income distributions to Italian resident beneficiaries by certain opaque foreign trusts has resolves some problems of an interpretative nature, but, at the same time, presents some grey areas.

In summary, the new provisions provide that amounts or values paid by opaque trusts (and similar arrangements) established in a low tax jurisdiction are taxed in the hands of the Italian resident beneficiaries as capital income (pursuant to art. 44, paragraph 1, letter g-sexies) of the Income Tax Code), contributing to the formation of the taxable income of the beneficiary itself, and therefore subject to the progressive income tax rates (23-43%).

The aforementioned Article 13 introduces also a presumption in favor of the tax authorities according to which the entire amount distributed by foreign trusts and similar arrangements to Italian resident beneficiaries qualifies as income in case it is not possible to distinguish between income and capital.

A first issue that would require a clarification concerns the term "established", which should in principle refer to the residence of the trust, generally coinciding with the tax domicile of the trustee. However, for example, the hypothesis of co-trustees needs to be clarified.

For instance, the presence of more than one trustee is quite common in the United Kingdom, where, if the settlor is not UK resident and domiciled (at the time the trust is set up and any additional contributions are made) and there is at least one trustee who is not resident or domiciled in the United Kingdom, the trustees (considered a single deemed person) are not considered to be resident in UK, irrespective of whether there is a majority of UK trustees or whether the trust is administered in the United Kingdom.

Therefore, in the case of a committee of trustees, consisting of two UK trustees and one resident abroad, the UK tax authorities would not issue any certificate of tax residency despite the administration is located in the United Kingdom. In the event

that the Revenue Agency clarifies that the term "established" coincides with the concept of tax residency set forth in Article 73 ITC, and therefore in principle with the seat of the trust's administration, there could be situations where the trust - for the purposes of the new law provisions - would not be resident, in a low tax jurisdiction, even though the trust has the typical preferential tax treatment reserved to offshore trusts.

Another aspect that presents some interpretative difficulties is the identification of low tax jurisdictions, which are to be determined by referring to Article 47-bis of the ITC. The latter, as well known, provides a different criterion for the identification of low tax jurisdictions: the comparison of effective taxation levels in the case of a controlling interest or the comparison of nominal tax rates in the absence of control (the concept of control is to be intended according to Article 167 of the ITC which regulates the CFC regime).

Transferring the provisions of Article 47-bis to the trust, the Position Paper of Step Italy agreed that for the purposes of comparing the level of taxation, reference should be made to the nominal tax rates; this is due to the impossibility of combining the concept of control referred to in Article 167, paragraph 2, TUIR (shares control and contractual control) to the trust.

On the same point, it is not clear which is the Italian tax to be taken as a reference for the purposes of comparing nominal levels of taxation. The most rational solution would be to take the IRES rate equal to 24% for non-commercial trusts, plus the IRAP rate equal to 3.9% for commercial trusts. However, in practice we frequently see the presence of "financial" trusts, whose income is subject, with the exception of dividends, to the substitute tax of 26%.

Finally, the mentioned Art. 47-bis excludes from the category of low tax jurisdictions the States or territories belonging to the European Union or to the European Economic Area with which Italy has stipulated an agreement which guarantees an effective exchange of information (Norway, Liechtenstein and Iceland). The exclusion of EU/EEA countries or not is not a minor issue. For example, any foreign source income received by a trust residing in Cyprus is not subject, under certain conditions, to any Cypriot taxation either by the trust or by non-resident beneficiaries. In this case, the exclusion of trusts established in

EU/EEA countries from the list of potential low tax trusts would lead to double non-taxation.

The example illustrated could indeed encourage the transfer of the seat of the trust administration in those jurisdictions.