

News Analysis: Court Reverses on Application of Penalties for Abusive Transactions

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While an obiter dictum is arguably not essential to the holding of a case decision and not binding on future courts, it might be persuasive. It is not uncommon for yesterday's obiter dicta to develop into today's tax law. That could be the outcome from a May 5 statement by the Italian Supreme Court of Appeal in Decision No. 12249 involving a corporation whose vast majority of shareholders were also members of an exempt organization.

The two entities entered into a contract under which the corporation granted the exempt organization a right to use a sports complex. The Italian Revenue argued that the contract had been entered into for the sole purpose of assigning to the exempt organization the corporation's otherwise taxable income from membership dues. The Supreme Court of Appeal held against the taxpayer. For procedural reasons, the Court did not rule on the penalty issue, but it said the penalty regime is not automatically inapplicable because of the transaction's lack of economic substance or otherwise abusive nature.

Generally, Italian tax civil penalties range from 100 to 200 percent of the additional tax assessed. The tax authorities seem to apply the penalties regardless of the abusive nature of the transaction, the disallowance of

(or the adjustment to) which generated the additional tax. Italian practitioners, on the other hand, tend to find the penalties either applicable only to the extent the law relevant to the transaction at issue is clear and unambiguous or inapplicable altogether.

The latter argument is based on the theory, backed by the European Court of Justice's decision in *Halifax* (C-255/02), that for a taxpayer who did not formally violate the law, the penalty is represented by the tax he is required to pay as a result of the tax authorities' adjustments to his taxable income.

Until Decision No. 12249, the Italian courts have generally followed this approach, and the Supreme Court of Appeal had itself rendered two decisions (No. 8487 of April 9, 2009, and No. 12042 of May 25, 2009) along these lines. The decision under review seems to be in sharp contrast with the Court's prior interpretations on this matter. (For prior coverage of Decision No. 8487, see *Doc 2009-10106* or *2009 WTD 85-9*.)

Accordingly, for taxpayers who engaged in transactions that on examination the tax authorities find abusive, the only relief from penalties seems to be that provided by article 8 of Decreto Legislativo (Legislative Decree) 546/92, under which penalties may not apply to the extent the precise application of the tax laws to a taxpayer's particular situation at the time of the investment decision is uncertain. ◆

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