

San Marino tax reform

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The Republic of San Marino, situated on the Italian peninsula, is the oldest surviving sovereign state and constitutional republic in the world and also one of the wealthiest countries in terms of GDP (per capita). It is also a highly stable economy and this article illustrates the country's tax system and treaty network, which has been progressively expanding over the last four years. Although not a member of the EU, the Republic is taking initiatives towards strengthening relations with the European countries.

I. Introduction

Within an international economic context marked by a strong climate of uncertainties and characterised by a worldwide crisis, small states such as the San Marino Republic are obliged to face a complex challenge relying only on means that are notably limited. There is a need to promote one's economy at an international level with the aim to attract investors within a scenario that proposes a set of international principles and rules that are thoroughly amended and strongly oriented towards greater transparency and co-operation. Micro-states must therefore, on the one hand “shed” the “*tax haven*” label by aligning their own legislation to international transparency and co-operation standards, and on the other, promote their economies through competitive elements that are compatible with the needs of the international community for the keeping of a sustainable balance of tax rules and conditions in cross-border economic relations, foregoing thus the competitive advantages that might have derived from the tax differential and from confidentiality.

The said challenge becomes especially difficult in view of the fact that small nations have less economic resources than larger nations and are more vulnerable to internal economic trend fluctuations. A shortage of economic resources, as a result of a changing

economy, requires a strong determination in the awareness that today's “*sacrifices*” might become tomorrow's new wealth when the economy will be able to realise greater benefits through increased integration with the economy of other states, thanks to a framework of internal rules and international agreements that render it “*compatible*” with the economies of other states.

II. San Marino's tax treaty network

Double tax conventions represent the legal/juridical basis to regulate tax aspects involving economic relations between two countries and, in addition to ensuring the necessary information exchange for the purpose of avoiding distorting phenomena, allow to establish a clear framework of rules within which entities of one contracting state may carry out cross-border activities. Having full cognizance of such a significant opportunity, the San Marino Government has – during this past four-year period – vigorously activated the treaty network consisting of DTAs (i.e., Double Tax Agreements) and TIEAs (i.e., Tax Information Exchange Agreements) pursuant to the most recent OECD standards. Although TIEAs might have a scope that is strictly limited to the exchange of information, signing them represents, in many cases, a first

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step towards the establishment of bilateral relations with a foreign state with the purpose of consolidating relations through the subsequent signing of a double tax convention.

III. Membership of the European Union – benefit or disadvantage?

In line with such strategic vision, the San Marino Republic succeeded, in the last few years in instituting a significant dialogue with the European Community in order to promote the necessary initiatives to give new life to relations with EU countries on a multilateral basis. Small European states which, to date, are not EU members – and among these, in addition to San Marino, we also find Andorra and Liechtenstein – are often faced with the difficult choice of whether or not to join as an EU member, especially in the light of the current economic European context where, on the one side, keeping one's own distinctive features might be an advantage, while non-participation might simultaneously also involve considerable disadvantages such as the impossibility of being part of an integrated economic system. Leaving aside the afore-mentioned "costs/benefits" analysis, what becomes especially important for a state such as San Marino is the enforcement of economic/financial agreements entered into with the EU that allow a certain degree of integration of its own economy with the European economy, even if not a member state thereof. Such need has always been strongly felt by the various Sammarinese governments that succeeded each other, and the signing of two important agreements, namely, the Monetary Convention and the Agreement on Cooperation and Customs Union allowed, in time, to provide important answers on the development of commercial relations with Europe. On the one hand, San Marino ensured that the Euro be adopted as its official currency, avoiding thus some kind of "currency-related" isolation from the other European countries and on the other, it established a Customs Union with EU states which allowed free exchange of goods in the absence of customs.

IV. Monetary Convention with the EU

In the spring of 2012, the San Marino Republic initiated a new Monetary Convention with the EU which replaced the former Convention of 2000, renewing San Marino's right to use the Euro as its official currency and thus commencing a six-year term for San Marino's national regulations with regard to the alignment with the main EU Directives in financial, anti-money-laundering and anti-forgery (coins and bank notes) matters. Such alignment, once achieved, is expected to most certainly create the basis for further and rather significant developments towards integration, which, although not formal, may be realised in conjunction with Europe. Some of these could be reflected in the form of direct participation to the European payment system, similar to those followed by the states belonging to the EEA, including the possibility to have access to certain monetary policy tools, such as refinancing with the ECB. In particular, this last aspect represents a fundamental step towards the enhancement of instruments to overcome the negative

phases of the economic cycle. Lastly, it should be observed that the alignment to the main standards in regulatory matters of the European financial system represents a key driver in order to attract foreign investors and, in more general terms, to enter into mutual agreements with the single countries for the purpose of carrying out financial activities, thus expanding the market of Sammarinese operators, given that these latter suffered from a considerable contraction, also due to the policies adopted by the single states (and, for San Marino in particular, by Italy) aiming to curb capital drains and above all, encouraging repatriation of capitals that had already been channeled abroad.

The stipulation of conventions and treaties, in these last few years, is not the only evolution that the San Marino Republic has been experiencing within the context of international relations. Today, more than ever, the securing of international relations is strongly affected also by the development of the single states' links with the main international organisations. Evaluation policies and procedures adopted by such organisations are bound to impact the development of bilateral relations; hence the constructive approach of such evaluations increasingly becomes an essential condition to achieve the stipulation of agreements in order to promote and protect investments as well as for the stipulation of bilateral tax agreements.

V. Exchange of information

Notwithstanding the fact that San Marino is not an OECD Member, it joined the Global Forum on Transparency and Exchange of Information in 2001 and, starting from 2009, it also joined the OECD's evaluation process on the states' capacity to effectively implement the exchange of information, by means of the Peer Review Group. The said evaluation process in two phases is currently involving San Marino in the so-called "Phase 2" of the Peer Review Process on the effectiveness of information exchange, subsequent to the successful achievement of the previous phase which had the purpose of ascertaining the existence of regulatory conditions required to ensure information exchanges. To such effect, further to the consolidation of the Treaty Network, a number of internal regulatory interventions, carried out in the course of the relevant legislature, created the right conditions to successfully accomplish the so-called "Phase 1" among which the most important are represented by the 2011 laws on information exchange matters which, on the one hand, regulate roles and competencies of the various authorities in charge of information exchanges, and cooperation exchanges, on the other. In such kind of context, the provision – establishing the non-opposition of the banking secret vis-à-vis information requests by foreign authorities, on the basis of Article 26 of the OECD Model Tax Convention and of the OECD TIEA Model – is especially meaningful.

VI. Position within international community

Always within the framework of relations entered into with international organisations, San Marino, as Member of the Moneyval ever since 1998, successfully

passed the recent evaluations regarding compliance with international GAFI principles pertaining to countering measures against terrorism and money-laundering financing. Such important results, combined with the progress achieved by OECD evaluations, has effectively re-launched the image of the San Marino Republic within an international context and also served the purpose of significantly improving relations with its main commercial partners, i.e., Italy, which led to the signing, in June 2012, of the Amendment Protocol of the 2002 Double Tax Treaty. Such result represents, along with other agreements reached in the last few years, the basis for opening a new economic cooperation between the two states, overcoming those critical aspects that had provoked a stalemate in the relationship and heightened – at the level of the San Marino Republic – the effects of Italian policies aimed at countering tax evasion in general.

The absence of a double tax convention between Italy and San Marino did, in fact, engender a number of uncertainties in economic relations among enterprises of both states, thus giving rise, in particular, to some litigation issues involving tax-residence, inevitably exacerbated, as Italian evasion measures grew more stringent.

The analysis of the guidelines of the tax reform is clearly indicative of the “international reach” of the San Marino Tax Regulations which, after more than 20 years from the approval of the current framework are in need of a sweeping overhaul, also with regard to the necessity of economic internationalisation and therefore of the relevant tax aspects. In that respect, it

would be appropriate to underline the importance of certain specific features of the reform, such as the revision of the regulatory framework with regard to controls, audits and penalties, which is a clear signal by the San Marino Republic to give a stronger thrust to internal audits, for the purpose of countering tax evasion, including all such kinds of behaviours that might somehow jeopardise the Republic’s international relations. To such effect, the intent to counter the introduction of economic activities in San Marino for the simple purpose of “exploiting” the Sammarinese system to avoid taxes abroad is rather patent, the latter being a phenomenon that is harmful to a different degree but is nonetheless serious for both, the San Marino Republic as well as the source country.

VII. Conclusion

From a tax reform perspective, San Marino does not entirely leave aside the tax differential as a competitive advantage but rather “re-qualifies” it, aligning the same with the need for a balance required by the international community. San Marino intends to propose itself as an “economic hub” where taxation is still competitive, although in a “transparent” manner and this is represented not solely thanks to the effectiveness of controlling regulations and international cooperation tools but also to a more consistent alignment between nominal and effective taxation, creating a more efficient and virtuous system as a result.

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