

# Investment in Italy

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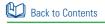
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# Investment in Italy

## Preface

**Investment in Italy** is one of the series of booklets published by KPMG to provide information of interest to those considering investing or doing business in the appropriate countries. This publication has been prepared by KPMG in Italy.

Every care has been taken to ensure that the information presented in this publication is correct and reflects the situation at 31 December 2016. Its purpose is to provide general guidelines on investing or doing business in Italy. However, the reader should be aware that the general framework of the legislation and the detailed regulations underpinning it are subject to frequent changes. Therefore, before taking specific decisions, further advice should be sought. If there is a significant lapse of time between determining a strategy and its implementation, any advice obtained which is critical to the strategy should be confirmed.

KPMG in Italy

#### December 2016 Seventh Edition



# 1. Country Overview

Italy, with a population of nearly 60 million inhabitants, is divided into 20 regions. Five of these regions (Valle d'Aosta, Trentino-Alto Adige, Friuli-Venezia Giulia, Sicily and Sardinia) have special autonomous status that enables them to enact certain pieces of local legislation.

The country is further subdivided into 101 provinces, 9 metropolitan cities and approximately 8,000 municipalities. In 2016, 27 new municipalities were created through mergers, while 73 were abolished.

Rome, located in the Lazio region, is the largest Italian city (with more than 2.8 million inhabitants). Milan in Lombardy (1.3 million inhabitants),

Naples in Campania (one million inhabitants), Turin in Piedmont (0.9 million inhabitants), and Palermo in Sicily (0.7 million inhabitants) are the other largest Italian cities.

The key business regions are located in the north of the country (Lombardy, Piedmont and Veneto).

The majority of the Italian population (64 percent) falls within the 15-64 age group. The percentage of people older than 65 is rising and currently stands at 22 percent, while the remaining 14 percent of the population falls within the 0-14 age group.

## 1.1 Transportation network

#### Airports



Italy has approximately 130 airports, handling over 157 million passengers and 985 thousand tonnes of freight per year.

One of its biggest international airports, Leonardo Da Vinci near Rome, handles more than 40 million passengers per year.

#### Railways



More than 800 million passengers and over 80 million tonnes of freight travel by rail each year.

Italy has one of the safest railway networks in Europe and boasts 16,752km of track. With the UK, it is the fourth largest in Europe after those of Germany, France and Poland.

High-speed rail services already connect the main Italian cities and are being extended further.

#### **Harbours**



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There are approximately 30 major ports, handling 45 million passengers and 443 million tonnes of freight per year.

There are another 148 ports distributed along approximately 7,400km of coastline.

#### Roads



The national road network includes approximately 180,000km of roads in total.

The national motorway network extends over 6,844km and makes up approximately 9 percent of the European motorway network.

### 1.2 Snapshot of the Italian economy

#### 1.2.1 Main macro-economic indicators for Italy: 2010-2016

|  | 2011    | 2012    | 2013    | 2014    | 2015    | 2016    | 2017    |
|--|---------|---------|---------|---------|---------|---------|---------|
| Real GDP<br>(EUR billion)                  | 1,614.4 | 1,568.3 | 1,540.9 | 1,543.5 | 1,553.0 | 1,567.5 | 1,578.5 |
| GDP (YoY changes)                          | 0.7%    | -2.9%   | -1.7%   | 0.2%    | 0.6%    | 0.9%    | 0.7%    |
| Unemployment rate<br>(% labour force)      | 8.4%    | 10.6%   | 12.2%   | 12.7%   | 11.9%   | 11.6%   | 11.4%   |
| Average nominal<br>wages inflation         | 2.4%    | 2.3%    | 2.1%    | 2.5%    | 2.5%    | 0.5%    | 1.7%    |
| Consumer price index                       | 2.9%    | 3.3%    | 1.3%    | 0.2%    | 0.1%    | -0.1%   | 0.7%    |
| Export of goods and services (% change)    | 6.1%    | 2.0%    | 1.0%    | 2.6%    | 4.0%    | 1.1%    | 1.4%    |
| Import of goods and<br>services (% change) | 1.2%    | -8.3%   | -2.2%   | 3.2%    | 5.9%    | 1.7%    | 1.5%    |

Source: Economist Intelligence Unit

#### 1.2.2 Key industries overview

The Italian economy is characterised by 4.4 million highly dynamic firms operating in a number of different industries. The vast majority are small and medium-sized enterprises (SMEs), of which more than 200,000 have over 10 employees. Only 3,500 are large companies with more than 250 employees. While the presence of a vast majority of SMEs is a common feature of many European economies, a defining feature of Italian industry specifically is the presence of a large number of micro-firms: approximately 95 percent of companies have fewer than nine employees, 4 percent of companies have 10-49 employees, and approximately 0.6 percent of companies employ more than 50 people (source: ISTAT, 2016). Italy can be geographically split into an industrially developed northern region dominated by private companies, and the less developed south, where there is a high rate of unemployment.

The service sector is a major contributor to the Italian economy. It accounts for approximately 74 percent of GDP and is also the fastest growing segment. Tourism, retail and financial services represent a significant part of the sector.

The industrial sector accounts for 18.8 percent of GDP, with the remainder contributed by agriculture (source: *L'Italia in cifre*, ISTAT, 2016). Motor vehicles, fashion and luxury goods, life sciences, aerospace, chemicals, information and communication technology, logistics, renewable energy, and precision machinery are among the most important Italian manufacturing sectors.

Some of the key Italian sectors are described below.

#### Tourism

With more than 33,000 hotels across Italy, tourism is one of the driving forces of the Italian economy, with foreign travellers spending approximately EUR 35.5 billion in 2015 (+3.8 percent YoY). Thanks to Italy's remarkable artistic, historic and cultural heritage, combined with its internationally acclaimed excellence in wine, food and natural landscapes, the country offers enormous potential for growth and exceptional investment opportunities.

Excellent investment opportunities are to be found in accommodation, infrastructure and services, such as transport and reception facilities (restaurants, shops and leisure facilities).

In 2015, Rome was the main tourist destination in Italy with nearly 25 million stays (+4.6 percent on 2014), followed by Milan (11.7 million, +14.7 percent, mainly due to Expo), Venice (10.2 million), Florence (9.1million), and Rimini (6.9 million).

#### Automotive

In 2016, the national market grew by 15.8 percent on 2015, with 1.82 million passenger cars sold/registered. Approximately 29 percent of passenger car sales were made by FCA, while the highest selling premium brand was Mercedes. The three best-selling models in Italy in 2016 were the FIAT Panda, Lancia Ypsilon, and FIAT 500L.

Data collected in October 2016 confirmed the recovery of the national automotive industry, specifically in relation to vehicles and engines (+3.1 percent), vehicles and trailer bodies (+8.4 percent), and Original Equipment Manufacturers (OEMs) (+3.2 percent).

This sector is a star performer in the Italian manufacturing arena, thanks especially to the presence of large car-manufacturing companies (such

as Fiat, Ferrari, Alfa Romeo, Lancia, Lamborghini, and Maserati) and other motor vehicle manufacturers (Aprilia, Ducati, and Piaggio), which create a significant allied economy among SMEs.

#### Fashion and luxury

With revenues of approximately EUR 84 billion, Italy has the most active fashion and luxury industry in the world, and without a doubt, it represents one of the most economically influential sectors of the Italian economy.

In addition to the big names that dominate the market (e.g. Armani, Gucci, Prada, Dolce & Gabbana, Cavalli, Ferragamo, Ermenegildo Zegna and Bottega Veneta in high-end fashion, Bulgari in watches and jewellery, Luxottica and Safilo in eyewear, and firms such as Perini, Azimut and Ferretti in the yacht business), the market is characterised by a large number of SMEs (Kiton, Canali, Corneliani, Brioni in high-end fashion, Minotti and B&B in high-end furniture, etc.). These companies combine creativity with manufacturing skills, and contribute to the global image of the Made In Italy "trademark".

#### Pharmaceuticals

The Italian pharmaceuticals industry is worth approximately EUR 30 billion, 73% percent of which is due to exports (EUR 22 billion). 60 percent of pharmaceutical companies in Italy are foreign-owned, for example GlaxoSmith&Kline, Novartis, and Baxter, while the remaining 40 percent are Italian-owned, for example Recordati, Zambon, Angelini, Bracco, and Sigma-Tau. In 2015, investments in this sector totalled EUR 1.4 billion, and its workforce comprised 63,500 employees, 90 percent of whom were graduates.

The strong performance of exports in this sector is the result of the increased quality of medicines and vaccines being exported all over the world: between 2010 and 2015 the average value of exports grew by 34 percent (compared to 22 percent across the EU).

#### Information and communication technology

The Italian ICT market grew by 1.0 percent to be worth EUR 64.9 billion in 2015, reversing the decline seen in 2014. The main growth drivers were software, services and innovation. All sectors contributed to the recovery, with the exception of telecommunications network services, the largest individual sector, which fell 2.4 percent in value to EUR 22.6 billion, as a result of declining tariffs. The second largest segment, devices and systems, grew by 0.6 percent to EUR 17.0 billion. This was followed by information technology services at EUR 10.4 billion, up 1.5 percent, whilst digital content and advertising was worth EUR 9.0 billion, up 8.6 percent. The value of the software and ICT solutions segment rose by 4.7 percent to 6.0 billion.

#### Chemicals

The Italian chemical industry has a production turnover of approximately EUR 52 billion, making Italy the third biggest chemical producer in Europe with a market share of 10 percent. It is characterised by the stable presence of many leading foreign companies. The quality of Italian research and its widely recognised scientific expertise are an important attraction, especially in fine chemistry and specialised chemistry. Manufacturing companies are a good mix of sizes: medium-sized and large Italian companies (including Versalis, the Mapei Group, the Mossi Ghisolfi Group and RadiciGroup) account for 24 percent of production, multinationals (e.g. BASF, Bayer, Air Liquide, and Linde) for 37 percent, and SMEs for 39 percent.

#### Aerospace

With an annual turnover of EUR 13 billion, 7 billion of which is due to exports, and a workforce of over 52,000, the Italian aerospace industry ranks seventh in the world and fourth in Europe. The Italian aerospace & defence field includes leading parties to important international cooperation agreements.

Piedmontese technical-productive specialisation, both in manufacturing and technical services, is well known for developing aircrafts, motors, propellers, satellites, infrastructure, and ground and on-board control systems. The high level of innovation and research lead to the realisation of 3 pressurised modules for transporting cargo to the International Space Station – Leonardo, Donatello and Raffaello –, which were designed and manufactured in Turin.

#### Renewable energy

Italy is one of the most virtuous of the EU Member States in terms of renewable energy policies and measures. By 2013 Italy had already reached and exceeded the energy level consumption target planned for 2020 (158 million tonnes); at 17.1 percent, it has already reached the goal of achieving 17 percent of its gross final consumption of energy from renewable sources by 2020. Furthermore, Italy has the fifth biggest total installed capacity of wind energy in Europe (approximately 9 GW, a 6.3 percent market share). Moreover, it should be borne in mind that renewables will continue to play a key role in helping the EU meet its energy needs beyond 2020. EU countries have already agreed on a new renewable energy target of at least 27 percent of final energy consumption in the EU as a whole by 2030 as part of the EU's energy and climate goals for 2030.

#### 1.2.3 The role of industrial clusters

Italy has 162 industrial clusters. Industrial clusters are a strategic feature of the Italian industrial system and for some industries, are the backbone of 'Made in Italy' and the essence of the manufacturing sector. The last 15 years have seen progressive and marked growth in the number of clusters, favoured by national and regional legislation and by the average small size of Italian companies, which pushes them to create organic and geographically close conglomerates within the same supply chain/ industry.

The Italian network of industrial clusters, which is based on the interdependence and cooperation between SMEs located in a specific local area, has historically been one of the strengths of the Italian economy, contributing significantly to the growth of income and employment and ensuring products of the highest quality and originality.



Source: ISTAT, Distretti Industriali Italiani, Osservatorio Nazionale Distretti Italiani

1.2.4 Typical issues facing Italian medium-sized companies

#### Broad variety of legal forms

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Italian law offers a variety of legal forms (e.g. corporations, partnerships), which are subject to specific tax rules and corporate laws. The legal form of a medium-sized company may reflect the stage of development of a business, in that partnerships are typically used for very small or family-run businesses, and are converted into corporations when they grow larger or new shareholders arrive. Changes in Italian tax regulations and the degree of personal risk assumed by shareholders/owners also have an impact on the choice of legal form.

#### Separation of operating and holding companies

In Italian medium-sized businesses, entrepreneurs tend to keep their business assets separate from other assets such as financial investments or real estate assets, using different legal entities and holding companies. These structures are often tax driven, although risk management also plays a role. Potential investors should give careful consideration to the fact that targets of potential acquisitions may or may not include, for example, real estate assets or companies, and that the capital requirements may therefore vary significantly.

#### Main shareholder/owner involved in the business

Italian medium-sized companies are often family-owned and run businesses: as such, they are often reliant to a significant degree on the involvement of the shareholder/owner. Certain 'discretionary' transactions are not infrequent, whilst future operating results may depend strongly on the continued presence of this key person.

#### Requirements for audited financial statements

The audit requirement is dependent on the size of the company (measured by equity, assets, sales and number of employees): therefore, the financial statements of a large number of Italian medium-sized companies are not audited. In addition, the accounting of medium-sized companies is frequently tax driven in a constantly changing tax scenario.

Potential investors should always obtain a thorough financial, tax and legal due diligence review and make use of tax structuring assistance to identify contingent liabilities.

#### Language

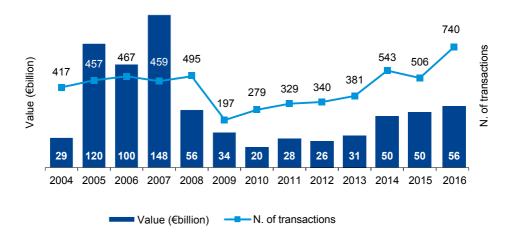
Financial, legal and tax information is generally prepared in Italian and based on Italian GAAP. A potential investor should consider that financial information may differ if reported under the GAAP of other jurisdictions.

#### Employee issues

Employees are generally highly knowledgeable, experienced and skilled as a result of the Italian system of in-house apprenticeships and vocational studies. Employee remuneration is commonly subject to collective bargaining agreements enforced by strong trade unions. A potential investor should be fully aware that certain company or group restructurings are subject to an agreement with the relevant trade union.

# 1.3 Private investment in Italian companies

Italian mergers and acquisitions from 2004 to 2016: value and number of transactions



Source: KPMG Corporate Finance (1) Pre Consolidated data

1 Note: The CDP is a joint-stock company, 80.1 percent of the share capital of which is owned by the Italian Ministry of Economy and Finance, with 18.4 percent held by various bank foundations and the remaining 1.5 percent in treasury shares.



Due to the weak economic outlook and the credit crunch, in 2008 the M&A market reported the lowest number of transactions in four years, falling further in 2009.

After a period of public investment, mainly through the "*Cassa Depositi e Prestiti*" (CDP)\*, 2014 was a year of corporate reorganisations involving several leading Italian groups.

In 2016, the M&A market showed solid growth (gaining in value by 25 percent). After a record number of IPOs in 2015, with 30 new listings, 2016 saw 15 new listings.

Overall, in 2016 the Italian M&A market confirmed its stable overall value of transactions (EUR 56 billion, +4 percent on 2015).

The improved general economic climate and conditions of the European and Italian financial markets helped to strengthen the confidence of Italian operators and the interest of foreign investors in Italy.

Italian-managed transactions abroad stood at a record number of 142, with a value of EUR 13.5 billion (in 2015 there were 97, with a value of EUR 10.2 billion.

Foreign M&A transactions in Italy dropped to 240, with a value of EUR 18.9 billion, representing around one-third of the total (in 2015 foreignmanaged transactions in Italy represented 57% of the total).

93 Italian companies were acquired by Private Equity Funds in 2016 (50 by Italian PE Funds, with a value of EUR 2 billion, and 43 by foreign PE Funds, with a value of EUR 4.4 billion).

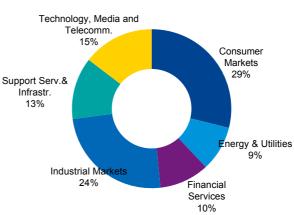
#### 2016 M&A values by industry (target company)

Technology, Media and Telecomm. 8% Support Serv.& Infrastr.13% Industrial Markets 13% Financial Services 38%

Total value: EUR 55.9 billion \*

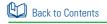
Source: KPMG Corporate Finance (\*) Pre Consolidated data

#### 2015 M&A number of transactions by industry (target company)



Total number: 740 transactions \*

Source: KPMG Corporate Finance (\*) Pre Consolidated data



# 2. Incentives for investors

### 2.1 Overview

The investment plan for Europe (also known as the 'Juncker Plan') aims to mobilise at least EUR 315 billion in private and public investment over three years (2015-2018). Its goals are:

- to boost investment;
- to increase competitiveness;
- to support long-term economic growth in the EU.

The plan was proposed by the European Commission in November 2014, following the Council of the European Union's call in June 2014 to address low levels of investment in the EU and boost growth and employment.

The Commission issued the plan's first legislative proposal – a draft regulation on the European Fund for Strategic Investments (EFSI) – in January 2015. The Council started working on the regulation on 19 January 2015.

The Council adopted its negotiating position on the proposed regulation (the Council's general approach) in March 2015, and began negotiations with the European Parliament on the final version of the proposal on 23 April 2015.

The Council adopted the regulation on 25 June 2015, following approval by the European Parliament on 24 June. The EFSI Regulation entered into force at the beginning of July 2015.

Italy is pressing ahead with new projects and new joint ventures with European partners to increase its share of the EUR 315 billion in funding promised by the Juncker Plan for Europe. Italy needs to secure guarantees from the EFSI in order to increase its loans from the EIB (European Investment Bank) and EIF (European Investment Fund), and for financing for riskier Italian projects.

The investment plan for Europe has three parts to it:

- setting up a European fund for strategic investments;
- · ensuring that investment finance reaches the real economy;
- improving the investment environment.

#### 1. The European Fund for Strategic Investments

The Fund uses public funds to mobilise additional private investment. It gives credit protection to the financing provided by the EIB and the EIF. The Fund was established as an account managed by the EIB.

The EFSI focuses on investment in a broad range of sectors, including infrastructure, energy, research and innovation, broadband and education. It also supports SMEs (mostly via the EIF).

The Fund consists of a EUR 16 billion guarantee from the EU budget and EUR 5 billion from the EIB.

The Fund – EUR 21 billion in total – is expected to achieve an overall multiplier effect of 1:15, and thus generate up to EUR 315 billion in investments in total.

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#### New proposal on the EFSI

In December 2016, the Council finalised its negotiating position on a new proposal for a regulation extending the term of the fund until 31 December 2020 and introducing a number of technical improvements to the fund and the European Investment Advisory Hub (EIAH).

In addition to extending the fund's term, the key changes to the EFSI agreed by the Council include:

- increasing the investment target to EUR 500 billion;
- increasing the EU budget guarantee to EUR 26 billion (EUR 16 billion of which will be available for guarantee calls until mid-2018);
- increasing the European Investment Bank's contribution to EUR 7.5 billion (from the current EUR 5 billion).

Furthermore, improvements aim to ensure that the fund's support covers as many EU countries as possible, and that it finances a wider range of sectors than before, such as agriculture, forestry, fisheries and other parts of the bio-economy, as well as climate-related actions. The Council will begin discussions with the European Parliament on the final version of the draft regulation when the Parliament has finalised its negotiating stance.

#### 2. Ensuring that investment finance reaches the real economy

The European investment project portal and a European investment advisory hub (EIAH) have been established to help investment finance reach the real economy.

The hub provides technical assistance and support. It bundles together existing EIB technical assistance programmes and provides additional advisory services for cases not covered by these.

The project portal helps potential investors to find information about each project and investment opportunities.

In December 2016, the Council finalised its negotiating position on a proposal to introduce technical improvements to the EIAH.

The proposal aims to make it easier for the EIAH to provide more targeted technical assistance at local level across the EU. It also aims to make it easier to combine EFSI financing with support from other sources of EU funding, including European structural and investment funds.

#### 3. Improving the investment environment

The aim is to boost investment by improving the business environment and easing access to finance, especially for SMEs.

The overall objective is to remove barriers to investment and create simpler, better and more predictable regulation in the EU, especially in infrastructure, where investments span several years or decades.

To help improve financing conditions in the EU, the plan envisages the creation of a 'Capital Markets Union' to reduce fragmentation in the financial markets and increase the supply of capital to businesses and investment projects.

In December 2016 the Council adopted conclusions on a number of issues affecting investment in the EU, identified by the Economic Policy Committee. The conclusions should influence the recommendations made to the Member States under the European Semester, the EU's policy monitoring process.

#### **Results so far**

In its first 18 months, the EFSI stimulated EUR 138.3 billion in new investments in 27 Member States. 290,000 SMEs and mid-cap companies are expected to benefit, gaining better access to finance.

In Italy, 28 projects have been approved for an amount of nearly EUR 3 billion. This is expected to generate over EUR 8.5 billion in investments. With regard to SME financing, under EFSI, the EIF has approved 40 agreements with financial intermediaries (banks, funds, etc). The financing totals over EUR 1.3 billion and is expected to generate nearly EUR 20.2 billion in investments. Some 191,000 smaller companies and start-ups are expected to benefit from the support.

# 2.2 Main incentives offered by the Italian government

#### 2.2.1 Contratto di Sviluppo

Development Contracts (Contratti di Sviluppo) provide incentives for major investments in industry (including in businesses that process and sell agricultural products), tourism, and environmental protection, and Back to Contents 🖳

in R&D and innovation. The total minimum investment required is EUR 20 million, exclusive of infrastructure expenses. For businesses that process and sell agricultural products, the amount is reduced to EUR 7.5 million. The investment programme must be concluded within a maximum period of 48 months from the date of approval of the request for financing.

Development Contracts are targeted at Italian and foreign large, medium and small enterprises. The recipients of the subsidies are:

- the applicant company, which is responsible for technical and financial compliance with the Contract and is also the formal point of contact for Invitalia, including on the behalf of other companies involved;
- any companies that implement investment projects under the Development Contract;
- the participants in any research, development and innovation projects;

Development Contracts deliver the following financial benefits (including in combination):

- non-repayable grants towards facilities;
- non-repayable grants towards expenses;
- subsidised financing;
- interest subsidies.

The amount granted depends on the type of project (investment or research; development or innovation), the location of the initiative, and the size of the company. There are different incentives for projects with environmental aims.

#### 2.2.2 "Industria 4.0" national plan

The expression "Industry 4.0" refers to the so-called "fourth industrial revolution." Made possible by the availability of low-cost sensors and wireless connections, this new industrial revolution is characterised by an increasingly pervasive use of data and information, computerised technology and data analysis, new materials, and totally digitised and interconnected components and systems (the Internet of things and machines).

Italy has developed the "Industria 4.0" National Plan, which includes practical measures developed along the following main guidelines:

- operate in technological neutrality;
- implement horizontal actions, avoiding vertical or sector-based ones;
- work on enabling factors;



- steer existing instruments to promote technological leaps forward and productivity;
- coordinate key stakeholders without acting as a controller or decisionmaker;

The plan follows four strategic lines:

- innovative investments: stimulate private investments in I4.0 technology drivers and increase private expenditure in research & development & innovation;
- enabling infrastructure: ensure adequate network infrastructure and the security and protection of data, cooperate in establishing the IoT (Internet of things), open standards and interoperability criteria;
- expertise and research: develop skills and stimulate research through ad hoc training courses;
- awareness and governance: generate interest in I4.0 opportunities and create shared public-private governance policies.

### 2.2.3 The National Operational Programme for Research and Innovation

The programme aims to promote the growth of transition regions – Abruzzo, Molise and Sardinia, and less developed regions – Basilicata, Campania, Calabria, Puglia and Sicily, by allocating a total of EUR 1.698 billion.

In line with the strategic framework of the Smart Specialisation Strategy (S3) and the National Programme for Research Infrastructures (PNIR), it is structured around 12 fields of application: Aerospace; Agrifood; Blue Growth (sea economy); Green Chemistry; Design, Creativity and Made in Italy (not R&D); Energy; Smart Manufacturing; Sustainable Mobility; Health, Secure and Inclusive Communities; Technology for Life Environments; and Technologies for Cultural Heritage.

The programme focuses on:

- investing in education, training and vocational training for skills and lifelong learning by developing education and training infrastructure;
- strengthening research, technological development and innovation.

The main areas of investment to be supported under the programme include:

 promoting business investment in research and innovation (74 percent of the total resources);

- investing in education, training and vocational training for skills and lifelong learning by developing education and training infrastructure (22 percent);
- technical assistance to support the implementation of the programme (4 percent).

#### 2.2.4 Invitalia

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Invitalia is a reliable partner for foreign investors who wish to set up or expand their business in Italy. Its mission is to offer a single and reliable point of reference to current and new investors seeking to set up or expand their business in Italy. The Agency offers a wide range of tailor-made, free-of-charge and confidential services to foreign investors, including:

- pre-investment information;
- business set-up assistance;
- after care.

It does this through stable and structured cooperation with institutional and professional partners, such as regional government bodies, institutional partnerships, national and international banks (such as the China Development Bank, China Exim Bank, Bank of Tokyo-Mitsubishi UFJ, Mizuho Bank Ltd, Unicredit S.p.A., BNL Gruppo BNP Paribas, Banca Popolare di Sondrio, and Banca Intesa San Paolo).

Invitalia supports international action plans to promote investment opportunities in priority sectors, assisting companies in developing business solutions and strategic partnerships.

Invitalia manages Institutional Development Contracts on behalf of the Government, planning projects, evaluating them, and implementing procedures.

#### Minimum investment thresholds:

- EUR 20 million for industry (EUR 7.5 million for the agrifood industry);
- EUR 20 million for tourism;
- EUR 20 million for environmental protection.

#### Types of incentives

Grants and soft loans for capital investments and research and experimental development investments.

# 2.3 Main incentives offered by the regions

Regional policy has a strong impact in many fields. Regional investments help to meet many EU policy objectives and implement accompanying measures in education, employment, energy, the environment, the single market, and research and innovation.

In particular, regional policy provides the necessary investment framework to meet the goals of the Europe 2020 Strategy for smart, sustainable and inclusive growth in the European Union by 2020.

All Italian regions have issued specific laws providing business incentives such as:

- grants or subsidised loans to SMEs for capital expenditure and business creation;
- · aid to the service industry, trade and tourism;
- aid to local business sectors.

These incentives are often combined with local assistance and consulting services, provided by either local or international business development agencies or by regional financial companies.

Regional programmes are also implemented for the specific purpose of benefitting from the **European Regional Development Fund (ERDF)** and the **European Social Fund (ESF)**.

#### 2.3.1 The ERDF Regional Development Programme

Its aim is to finance infrastructure and manufacturing plants to create and safeguard sustainable jobs. The ERDF is aimed specifically at SMEs and provides various financing facilities, including venture capital, debt and guarantee funds, etc.

Areas of investment include the development of industrial sites, research and technology, information technology, protection of the environment, energy, education, equal opportunities, and transnational, cross-border and interregional cooperation.

The ERDF focuses its investments on the following key priority areas:

- innovation and research;
- the digital agenda;
- support for SMEs;

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- the low-carbon economy.

The amount of ERDF resources allocated to the priority areas mentioned above depends on the category of the region.

- In more developed regions (GDP per capita > 90 percent of the EU-27 average), at least 80 percent of funding must go on at least two of the priority areas.
- In transition regions (GDP per capita between 75 percent and <90 percent of the EU-27 average), this drops down to 60 percent.
- In less developed regions (GDP per capita <75 percent of the EU-27 average), this drops down to 50 percent.

Furthermore, the following proportions of ERDF resources must be channelled specifically towards low-carbon economy projects:

- in more developed regions: 20 percent;
- in transition regions: 15 percent;
- in less developed regions: 12 percent.

Under European Territorial Cooperation programmes, at least 80 percent of funds must be used on the four priority areas mentioned above.

The ERDF also pays particular attention to specific territorial characteristics. ERDF action is designed to reduce economic, environmental and social problems in urban areas, with a special focus on sustainable urban development. At least 5 percent of ERDF resources are set aside for this field, through 'integrated actions' managed by cities.

Areas that are naturally at a disadvantage from a geographical viewpoint (remote, mountainous or sparsely populated areas) benefit from special treatment. Outermost areas also benefit from specific assistance from the ERDF to address possible disadvantages caused by their remoteness.

#### 2.3.2 The ESF Regional Programme

The ESF is Europe's main instrument for supporting jobs, helping people get better jobs, and ensuring fairer job opportunities for all EU citizens. It works by investing in Europe's human capital – its workers, its young people and all those seeking a job. ESF financing of EUR 10 billion a year is improving job prospects for millions of Europeans, in particular those who find it difficult to get work.

The European Union is committed to creating more and better jobs and a socially inclusive society. These goals are at the core of the Europe

2020 strategy for generating smart, sustainable and inclusive growth in the EU. The current economic crisis is making this an even more demanding challenge. The ESF is playing an important role in meeting Europe's goals, and in mitigating the consequences of the economic crisis – especially the rise in unemployment and poverty levels.

The ESF drive to boost employment is aimed at all sectors and groups of people who can benefit. However, there is a focus on the groups that are worst off or can benefit significantly from ESF funding in the following areas:

- opening pathways to work;
- creating chances for youth;
- boosting business;
- caring for careers.



3 The incorporation or acquisition of a company: legal aspects

### 3.1 Foreign investors

Investments made in Italy by nationals of other European Union Member States are not subject to any limitations and are treated in the same way as those made by Italian nationals.

Foreign investments made by non-EU nationals are subject to the "reciprocity" condition: a foreigner may have the same rights as an Italian citizen if Italian citizens can carry out the same activities in the foreigner's country. Therefore, foreigners will enjoy the same rights that the national law of their own country allows to Italian citizens in that country.

Moreover, certain authorisations/requirements may be necessary for investments in some industries and regulated sectors (e.g. telecommunications and banking/financial intermediation) both for the incorporation and the acquisition of a company.

## 3.2 Company law

#### 3.2.1 General overview

Foreign investors who intend to conduct commercial activities in Italy can choose from a wide range of legal entities that may be incorporated under Italian law, depending on the company's organisational model, its commercial objectives, the level of capital to be committed, extent of liability and tax and accounting implications.

There are two main categories of legal entities:

- I. partnerships (società di persone), and
- II. companies (società di capitali).

The most important difference between these is that partnerships' assets and liabilities are only partially segregated from the assets and liabilities of their members, while companies' assets and liabilities are completely segregated.

A partnership may be set up in three different forms, as a:

- a. simple partnership (società semplice) this partnership may not be used to carry out business activities;
- b. general partnership (società in nome collettivo) in this partnership, all partners are jointly liable for all of the firm's debts and obligations; or
- c. limited partnership (società in accomandita semplice) this is a partnership with two different categories of partners: soci accomandanti whose liability is limited to the extent of their capital contribution; and soci accomandatari who are jointly liable for all debts and obligations of the partnership.

These kinds of partnerships do not have legal personality and the partners (with the exception of soci accomandatari) have unlimited liability.

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There are three different kinds of company that may be incorporated under Italian law:

- a. a joint-stock company (società per azioni or S.p.A.) in which the participants' equity is represented by shares;
- b. a limited liability company (*società a responsabilità limitata* or *S.r.l.*)
   in which the capital stock is represented by quotas as opposed to shares;
- c. a partnership limited by shares (*società in accomandita per azioni* or *S.a.p.a.*) this combines features of both limited partnerships and joint-stock companies. It is a company in which at least one member has unlimited liability, while the liability of the remaining members is limited to the extent of their capital subscriptions. Apart from this difference, an S.a.p.a. is similar to an S.p.A.

Below is a brief outline of the two main kinds of Italian companies: jointstock companies and limited liability companies.

#### 3.2.2 Joint-stock companies and limited liability companies

The basic principle governing both types of companies is that only the company is liable with its assets for its obligations: the liability of the shareholders/quotaholders is therefore limited to the amount paid in, or to be paid in, as corporate capital.

#### Joint-stock companies (S.p.A.s)

The two key features of an S.p.A. are the limited liability of all its members and the division of the capital into shares.

#### Corporate capital, shareholders and shares

A joint-stock company requires minimum share capital of EUR 50,000.00, of which at least 25 percent (amounting to EUR 12,500.00) must be paid upon in corporation.

For companies operating in specific fields (e.g. the insurance sector, banking, etc.) a higher amount of capital is required.

The minimum number of shareholders is one: in this case the share capital must be paid up in full immediately upon incorporation of the company. There is no maximum number of shareholders. Shareholders of an S.p.A. can be either natural or legal persons, Italian or foreign (see above).

The capital is divided into freely transferable (the company's articles of association may contain some limitations on the transferability of shares) and indivisible shares of equal value (the nominal value of each share corresponds to a fraction of the entire share capital), conferring equal rights, both administrative (e.g. voting rights) and economic (e.g. the right to a share of net profits). In addition to ordinary shares, the company's articles of association may provide for particular classes of shares granting special rights, also in respect of losses.

If permitted by the company's articles of association, capital contributions may also be represented by assets (either tangible, including receivables, or intangible). Contributions in kind must be fully paid in at the time of subscription and the contributor must provide a sworn appraisal of the assets by a court-appointed expert (in certain circumstances a simplified procedure for contributions in kind – without a sworn appraisal – is admitted). In no event can the overall value of the contribution be lower than that of the aggregate increase in share capital.

#### Governance

The "traditional" corporate governance model of an S.p.A. is based on:

- I. a shareholders' meeting;
- an administrative body (board of directors or sole director, appointed by the shareholders' meeting);
- III. a supervisory board (board of statutory auditors and registered audit firm, appointed by the shareholders' meeting).

At least one shareholders' meeting must be held each year, to approve the company's annual financial statements, no later than 120 days or, in exceptional circumstances, no later than 180 days after the close of the financial year.

Extraordinary shareholders' meetings must be held to approve matters such as amendments to the articles of association (including amendments to the corporate capital), the winding-up of the company (including the appointment of liquidators, their substitution and their powers), and mergers or similar corporate reorganisations.

The management of the company may be entrusted to a sole director or a board of directors, who handle all matters and transactions necessary or advisable for attaining the corporate object. Their management powers involve a duty to take all necessary and appropriate steps to attain the corporate object and to ensure compliance with the law, including the preparation of the draft annual financial statements.



S.p.A.s must also appoint a board of statutory auditors (*collegio sindacale*), formed of three or five statutory auditors and two alternate auditors. The main duty of the board of statutory auditors is to supervise compliance with the law and the articles of association. It must also verify that the company's organisational, administrative and accounting structures are adequate and work properly. Accounting controls are the responsibility of the board of statutory auditors or an audit firm.

Besides the "traditional" governance system described above, two further systems are available for S.p.A.s.

In the first (the *sistema monistico* or one-*tier* model, taken from Anglo-Saxon culture), management and control lies with a board of directors and a management control committee appointed amongst the members of the board. The management of the company is the exclusive responsibility of the board of directors, whilst the management control committee supervises the adequacy of the company's organisational structure, internal control system and administrative and accounting system. The committee also performs any additional functions assigned to it by the board of directors and, in particular, liaises with the auditors or board of statutory auditors with regard to accounting controls.

The second (the *modello dualistico* or two-*tier* model) provides for two corporate bodies: a management board and a supervisory board. The management of the company is entrusted exclusively to the management board, which must do everything necessary or advisable for attaining the corporate object. The supervisory board is entrusted with the functions of the board of statutory auditors and with those functions reserved, in the traditional model, to the shareholders' meeting.

Neither model includes a board of statutory auditors: accounting controls are carried out by a registered auditor (or an audit firm).

#### Limited liability companies (S.r.l.s)

This form of company is the most widely used in Italy because of its organisational flexibility and limited liability.

A limited liability company is suitable for companies with few quotaholders (even a sole quotaholder) and slim management structures.

#### Corporate capital, quotaholders and quotas

The minimum corporate capital for an S.r.l. is EUR 10,000.00 (with the exception of the minimum corporate capital for a "simplified S.r.l." as explained below), of which at least 25 percent (amounting to EUR 2,500.00) must be paid upon in corporation.

Law no. 99 of 9 August 2013 stipulates that the minimum capital of EUR 10,000 may also be built up over time ("progressive share capital") subject to certain statutory conditions, i.e. that every financial year the company allocates at least 20 percent of the year's net profits to the legal reserve.

The minimum number of quotaholders is one: in this case the corporate capital must be paid up in full immediately upon incorporation of the company. As with S.p.A.s, there are no restrictions on the number, residence or nationality of the quotaholders.

The corporate capital is divided into as many quotas as there are quotaholders; the quotas, unless indicated otherwise in the company's articles of association, are freely transferable. Rights, both administrative and economic, belong to quotaholders in proportion to the size of their stake in the company, unless the articles of association allow individual quotaholders special rights relating to the management of the company or the distribution of profits.

If expressly provided for by the company's articles of association, capital contributions may also be made in kind. Unlike contributions to the capital of joint-stock companies, those made to S.r.I.s can also consist of services supplied by the quotaholder.

#### Governance

The "traditional" model described above for S.p.A.s generally applies to S.r.I.s, with a number of simplifications and a large degree of flexibility.

Unless otherwise provided for in the company's articles of association, the management of a limited liability company must be entrusted to one or more quotaholders. Those quotaholders not involved in the management of the company are entitled to receive information from the directors and to consult and inspect, also through trusted professionals, the company's books and management documentation, and thus to monitor the directors' activities.

A limited liability company is not required (unless under specific circumstances provided for by law) to appoint a supervisory body: if the quotaholders decide to appoint a supervisory body (or if this is required by law), this can be a sole statutory auditor (*sindaco unico*) or a board of statutory auditors (*collegio sindacale*).

When a limited liability company is required to appoint a supervisory body, this is entrusted not only with the function of supervising compliance with the law and the articles of association, but also with the task of auditing the accounts, unless the articles of association or the law requires the company to appoint a registered auditor (or an audit firm).



#### Simplified S.r.l.s

Recently in 2013, in addition to the ordinary model, a new type of S.r.l. – a simplified limited liability company – was introduced to encourage entrepreneurship.

Its capital may not be lower than EUR 1.00 nor higher than EUR 9,999.99. The capital must be fully paid in cash to the management body at the time of the company's incorporation.

The quotaholders of a simplified S.r.l. may only be individuals (natural persons), not companies or other legal entities.

The articles of association of this new type of S.r.l. must be prepared according to a standard model prescribed by law.

No notarial fees are due to the notary for the incorporation of this kind of company.

#### 3.2.3 The main steps in incorporating a company

The main steps in the incorporation of an Italian company are as follows:

- I. drafting the memorandum of association: this records essential information about the company (notarial deed);
- drafting the articles of association: these contain rules for the operations and governance of the company (notarial deed);
- III. registration with the local VAT office: the new company must apply for a VAT no. and tax code as soon as it has been incorporated;
- IV. acquiring tax codes for the directors: the members of the board of directors, if foreign, must request Italian tax codes;
- V. registration in the Trade Register: the company acquires legal status after registration.

The process of constituting an Italian company can take from one to three weeks.

#### 3.2.4 Liquidation

A company can be dissolved and liquidated for one of the following reasons:

- it reaches the end of its duration, as established in its articles of association;
- the purpose for which it was established is achieved or can no longer be achieved;
- III. the shareholders'/quotaholders' meeting can no longer operate or remains inactive;
- IV. its capital falls below the legal minimum;



- V. its shareholders/quotaholders resolve (at an extraordinary general meeting) to liquidate the company (voluntary liquidation);
- VI. the company is unable to repay the stake of an exiting shareholder/ quotaholder;
- VII. any other reason established in the articles of association or by law.

Most of these grounds for dissolution are automatic (i.e. they do not have to be public knowledge and do not depend on a resolution or public record). When grounds arise, directors have a duty to ascertain the situation, record the event at the Trade Register and call a shareholders'/ quotaholders' meeting to appoint liquidators or remove the cause of liquidation.

If there is cause to wind up a company, the directors may not engage in particularly risky operations and must merely maintain the company's ordinary operations.

If there are grounds for winding up the company (e.g. loss of capital) and the directors or shareholders/quotaholders' meeting fails to take action, the court will appoint liquidators, at the request of the statutory auditors or individual shareholders/quotaholders.

The main function of liquidators is to dispose of the company's assets, pay off its creditors and prepare the final liquidation financial statements and a report specifying the amount, if any, of the proceeds from the liquidation available for distribution to each shareholder/quotaholder.

If the company's funds are insufficient to repay its debts and liabilities, the liquidators may ask the shareholders/quotaholders to provide the necessary resources, in proportion to their stake of the company's capital. No repayment of capital or earnings can be made before liquidation is complete, unless the accounts show that such payments will not prevent the full repayment of the company's creditors, or unless the shareholders'/quotaholders arrange appropriate guarantees.

Liquidation status may be revoked at any time by means of a shareholders/quotaholders' resolution and, where necessary, after the cause of liquidation has been removed.

The liquidation procedure is closed with the distribution of any proceeds from the liquidation to the shareholders/quotaholders. Immediately afterwards, the company is struck off the Trade Register (deregistration) and the books are filed with the court, which holds them for ten years.

#### 3.2.5 Representative offices and branches

Foreign companies have the right to establish the following in Italy:

- I. one or more representative offices, and/or
- II. one or more branches.

A representative office – which is not a legal entity of a foreign company in Italy – is characterised by a local presence to promote the company and its products/services and to perform other non-business operations (from a tax point of view, if the representative office carries on a business activity – such as selling goods, providing services, etc. – it is considered a permanent establishment).

A representative office is not required to keep books, publish financial statements or file income tax or VAT returns. It is, however, required to keep ordinary accounts in order to document the expenses (e.g. personnel costs, office equipment, etc.) to be covered by the foreign company's head office.

The establishment of a representative office must be registered with the Trade Register.

A branch is an extension of the foreign entity and depends – both administratively and economically – on its headquarters. It uses the same name and legal form as the foreign company: it does not have its own internal governing body but is managed directly by the governing body of the foreign company, which appoints one or more permanent legal representatives (*preposto/i*), who are entrusted with the powers to manage and represent the branch before third parties.

It does not have its own capital and is not required to draw up annual financial statements: a copy of the financial statements of the headquarters must be filed at the Trade Register.

An annual report is only required in order to prepare the Italian income tax return.

Contracts concluded by the branch through its legal representative are binding upon the foreign company and any liabilities for the breach of the contractual obligations are directly attributable to the latter.

The setting-up of a branch must be recorded in the Trade Register, together with the appointment of the legal representative.

### 3.3 M&A transactions

#### 3.3.1 General overview

Generally, M&A transactions involving existing companies can be carried out through the following structures:

- I. share/quota deals involving the purchase of shares (S.p.A.) or quotas (S.r.I.);
- II. asset deals involving the purchase of some or all of the assets of the target.

Share/quota deals and asset deals are not subject to general investment barriers, with the exception to the limitations described above for foreign investments.

Moreover, when the turnover of the undertakings involved in the acquisition exceeds certain thresholds, the transactions are subject to the prior notification of:

- I. the Italian Competition Authority, and/or
- II. the European Commission.

While in most instances the choice between a share/quota deal and an asset deal will be driven by tax-related considerations (see below), there are several purely legal implications to be taken into account in structuring a transaction, which need to be carefully addressed when drafting the relevant agreements.

#### 3.3.2 Share/quota deals

In a share/quota deal, the purchaser succeeds as shareholder/ quotaholder of the target. The purchaser becomes the owner of the legal entity and acquires the company's assets as well as all existing and potential liabilities and debts. It also takes over all the company's contracts, with all the related rights and obligations.

The main benefit of a share/quota deal is that it involves fewer formalities than an asset deal and provides greater certainty of continuity for the underlying business, with the notable exception of the effects of any "change of control" provisions in agreements entered into by the target company.

A change in the controlling interest of the target company does not determine a change of employer on paper, and there are no express legal obligations to notify or consult with trade unions in advance of the quota/share purchase, as is the case for the transfer of a business.



Another major advantage of a share/quota deal from the seller's perspective is that all liabilities remain with the company and therefore pass to the buyer upon transfer of ownership.

If the transaction does not involve 100 percent of the corporate capital, specific agreements with the shareholders/quotaholders regulating the governance of the target are advisable.

#### 3.3.3 Asset deals

In an asset deal, the purchaser acquires all the assets or certain business units of the target. It is important to define the object of the transaction (i.e. the assets, contracts, liabilities, workforces being transferred).

In asset deals, the following issues have to be taken into consideration.

- I. The purchaser and the seller become jointly liable towards creditors (despite any agreements between the parties that say otherwise) for all the debts of the business unit shown in the accounting records.
- II. The purchaser takes over all contracts (pertaining to the business) without prejudice to the right of the counterparty to terminate the contracts with reasonable grounds.
- III. The seller is bound by a non-competition obligation for a period of five years after the transfer.
- IV. If the transfer involves a company with more than 15 employees, a special procedure involving trade unions has to be followed (written notice must be sent to the unions at least 25 days before the agreement is signed).

#### 3.3.4 Takeover bids for listed companies

There are special rules for takeover bids for listed companies: if one buyer directly, indirectly or jointly acquires a stake of more than 30 percent in a target company listed on the Italian Stock Exchange, they must make a Public Offer or "Takeover Bid" (TOB) for the entire corporate capital of the target (a "Mandatory TOB").

The TOB price should be not lower than the highest price paid by the bidder over the last 12 months for any target share.

If no target shares have been purchased against payment in the last 12 months, the TOB price should be not lower than the market average over the previous 12 months.

The mains steps in a Mandatory TOB are:



- announcing the TOB: notification of the obligation to make the bid is sent to CONSOB (immediately);
- filing the bid documents: the bid documents are submitted to CONSOB for publication (no later than 20 days after the announcement has been made);
- III. CONSOB approves the bid documents (within 15 days of filing);
- IV. the TOB is published (immediately);
- V. the subscription period starts (not before 5 days after publication), which lasts between 15 and 25 days.

After the first TOB procedure, other steps may be taken to squeeze out minority shareholders, depending on the size of the stake acquired with the first TOB.

- a. If the stake acquired is less than 90 percent: the bidder may make a further TOB on the remaining shares, with no price constraints.
- b. If the stake acquired is between 90 percent and 95 percent: the bidder can place a minimum stake back on the market within 90 days to guarantee "sufficient" floating share capital or acquire the minority stake of any shareholder requesting to sell. The squeeze-out price is set according to CONSOB rules.
- c. If the stake acquired is equal to or more than 95 percent: the bidder (i) must acquire the minority stake of any shareholder requesting to sell; and (ii) will have the right to acquire any minority stake within 3 months and to delist the target. The squeeze-out price is set according to CONSOB rules.

## 3.4 Corporate criminal liability

Legislative Decree no. 231 of 8 June 2001 introduced corporate criminal liability into Italian law for specific types of offences.

A company can be held responsible if the offence:

- I. is committed in the interests of or to the advantage of the company, and
- II. is committed by persons who have a working relationship (directors, employees, etc.) with the company.

The crimes for which corporate criminal liability can be assessed are detailed in the decree. They include:

 a. offences against the public administration (such as corruption, embezzlement, etc.);

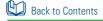
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- b. corporate crimes (such as the falsification of financial statements or prospectuses);
- c. offences involving market abuse;
- d. money laundering crimes;
- e. protection of health and safety in the workplace crimes;
- f. environmental crimes.

The assessment of liability may entail the application of pecuniary sanctions (up to a maximum of EUR 1.5 million; for multiple crimes connected to the same underlying action, sanctions may be increased threefold up to a maximum of EUR 4.6 million) and other penalties that may compromise the life of the company, including, inter alia:

- the suspension or revocation of authorisations, licences or concessions;
- II. the company's exclusion from public financing, grants or subsidies;
- III. the company being permanently disqualified from performing its activities

The company may be exempted from liability if it can prove that it has adopted and effectively implemented an Organisational, Management and Control Model suited to preventing offences (a "Model"), which details the key areas of risk and is supplemented by suitable disciplinary and treasury management operating procedures;

Moreover, the company must have given a specific body – the "Supervisory Body" (the members of which are chosen from a pool of qualified persons with a legal or accounting background on the grounds of their independence, professionalism, ethical standards and expertise) – with independent powers the duty of supervising the effectiveness of and compliance with the Model and keeping it up-to-date.



## 4. Accounting and reporting

## 4.1 Legal framework and regulations

Accounting and reporting are mainly regulated by the following laws and regulations:

- the Italian Civil Code;
- Italian tax codes;
- Italian Accounting Standards (local GAAP);
- International Accounting Standards/International Financial Reporting Standards, where applicable.

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## 4.2 Requirements

In Italy the double-entry method of bookkeeping is used. Records must be made in chronological order, without empty spaces or notes, and must not contain deletions; only where strictly necessary can text be crossed through in such a way that the letters remain legible. The general ledger must report all transactions on a daily basis.

The accounting books can also be kept on digital supports. There are specific provisions in place to guarantee the true date of entries. All books and records, even if they are computerised, must be kept for at least ten years after the date of the last entry, together with all related business correspondence.

## 4.3 Compulsory bookkeeping

#### 4.3.1 The general ledger

All the transactions performed by an Italian company must be recorded in this ledger in detail and in chronological order. Each entry must show the date of the transaction and include a brief description. All entries must be made within 60 days of the relevant transactions.

The general ledger must be consecutively numbered on each page, also showing the tax year (e.g. 2017/1, 2017/2, 2017/3, etc.). Stamp duty (currently EUR 16.00) is due at the beginning of every 100 pages.

Local software is normally designed so that each entry in the general ledger is also automatically recorded in the VAT registers.

Amounts in foreign currency cannot be converted at an average monthly exchange rate, since it is compulsory for tax and legal purposes to adopt the official exchange rate valid on the date of the transaction.

Accounts must be closed and reopened at the end of the financial year. The general ledger must be supported by ledger cards for each account (e.g. a 'bank deposit account XXY' ledger card; a 'cash 1' account ledger card; a 'client XYZ' ledger card). All the transactions that are chronologically recorded in the general ledger also have to be recorded in the ledger cards.

To summarise, the following details should appear:

- the progressive number of the transaction;
- the progressive number of the general ledger line;
- the date of the transaction;
- the code and/or title of the account;
- the nature of the transaction (not mandatory but recommended);



- · a brief description of the transaction;
- the third party in the transaction;
- the adjusting/closing/opening entries at the end of the year.

The end of each page should show the aggregate debit/credit amount to be carried forward to the next page.

To provide bookkeeping staff with comprehensive information, a petty cash book and a cheque disbursement book are also required.

#### 4.3.2 The inventory ledger

The inventory ledger must contain a description and valuation of the company's assets and liabilities as reported in the balance sheet.

#### 4.3.3 Business correspondence

The company must keep copies of all documents (letters, invoices, telegrams) sent and received in connection with each transaction. The copies must be stored in an orderly manner.

## 4.4 The language of accounting records

Civil and tax law does not expressly impose the use of Italian in the general ledger and VAT books. Therefore, using a foreign language for accounting records is not a violation of VAT and accounting rules.

However, according to the Italian Civil Code, books and accounting records may be used as elements of proof and put on record in court cases, and the law requires the Italian language to be used for legal documents in court proceedings.

Considering that the records may be presented to the tax authorities/ courts during assessments or litigation proceedings, it is thus advisable for them to be in Italian.

## 4.5 Keeping accounting records abroad

The Italian Civil Code and tax rules do not expressly prohibit a company from keeping its accounting records and compulsory accounting books outside Italy. However, the Italian Ministry of Finance clarified (in Tax

Ruling 167/E of 2000) that the accounting records of Italian companies belonging to multinational groups should be kept abroad. The accounts may be recorded and processed, in real time, using an electronic data processing (EDP) system located abroad, connected to the Italian subsidiary via telephone/satellite.

The accounting books must then be printed on the subsidiary's premises in Italy, where the data, books and supporting documentation must also be kept. It must also be possible to print accounting data already registered at any moment and in real time at the Italian company's premises.

In a tax inspection, the books, registers and accounting documents must be made available to the tax authorities immediately upon request. If the accounting books are not shown to the tax authorities upon request, the financial data may be considered unreliable and the authorities will have the right to assess income taxes and VAT on the basis of assumptions, without considering the company's actual results.

The Italian tax authorities also clarified (in Circular no. 45 of 19 October 2005) that invoices may be stored abroad in a digital system on the following conditions only:

- that there is a reciprocity agreement in place between the two states with regard to indirect taxation;
- that the Italian company can ensure automatic access to the archive at all times from its registered office;
- that the integrity and readability of the data is ensured during the whole period of storage;
- that all the documents and data stored in the digital system can be printed and downloaded onto another system.

## 4.6 The financial statements

The directors must draw up the financial statements after the end of the year. The statements comprise a balance sheet, profit and loss account, explanatory notes and cash flow statement.

The financial statements must be drawn up clearly and present a true and fair view of the assets, liabilities, financial position, and profits or losses of the company. If the information required by law is insufficient to give a true and fair view, additional information must be given.

If, in exceptional cases, the application of a rule is incompatible with a true and fair view, the rule must not be applied. The notes to the

financial statements must explain the departure from the rule and the impact this has on the representation of the assets, liabilities, financial position, and profit or loss.

Special rules on the format of financial statements are provided for companies operating in specific sectors. A short form and a reduction in the amount of information required are provided for "micro" and "small" enterprises.

4.7 International Accounting Standards/ International Financial Reporting Standards (IAS/IFRS)

#### 4.7.1 Differences between local GAAP and IFRS

According to Legislative Decree no. 38 of 28 February 2005, the following entities must adopt IFRS:

- listed entities;
- issuers of publicly traded financial instruments within the EU;
- banks and financial intermediaries whose business activities are supervised by the Bank of Italy;
- insurance companies.

Non-listed entities may adopt IFRS to prepare their separate financial statements provided that they do not have the option of drawing up their annual financial statements in the condensed from as per article 2435*bis* of the Italian Civil Code (companies whose securities are not listed on a regulated market may draw up their annual financial statements in the condensed from when, for three consecutive years, they have not exceeded two of the following limits: total assets: EUR 4,400,000.00; revenues from sales and services: EUR 8,800,000.00; an average of 50 employees per year).

Local GAAP and IFRS differ in many ways, varying in their degree of relative importance, and both sets of principles are subject to unpredictable regulatory changes. Therefore, should it be necessary to study their differences in any depth, this should be done when the information is needed and only under expert guidance. The table below is intended solely as a way of illustrating certain notions that could be of interest and therefore cannot be considered exhaustive.

| LOCAL GAAP   | IFRS   |
|--|--|
| Ger  | neral  |
| Similarly to under IFRS, a statement of cash flows is<br>required. The layout of the components of the financial<br>statements is provided by Company law. Similarly to under<br>IFRS, no extraordinary items are listed on the income<br>statements. They are disclosed in the notes. Restatements<br>of comparatives are not allowed. The effects of changes in<br>accounting policies and corrections of errors are included<br>in the income statements of the current year. In addition to<br>actions attributable to equity holders, net equity changes<br>only as a result of the profit or loss of the period. | A statement of cash flows is required.<br>IFRS do not prescribe a standard format for components of<br>the financial statements.<br>No extraordinary items are presented in the income<br>statements.<br>Changes in accounting policies and corrections of errors<br>could lead to restatements of comparatives.<br>In addition to actions attributable to equity holders, net<br>equity changes as a result of the profit or loss of the period<br>and income or expenses recognised directly as equity<br>(other comprehensive income).          |
| Consc  | lidation   |
| The existence of currently exercisable potential voting<br>rights is not taken into consideration in identifying<br>subsidiaries and associates.<br>Special Purpose Vehicles (SPVs) may be included in the<br>consolidation when the results of the SPV could affect the<br>investor.<br>Minority interests are not part of net equity.<br>Consolidation is required when two of the following limits<br>are exceeded in two consecutive years (Public Interest<br>Companies are excluded from this provision):<br>* Total Assets: EUR 20 million;<br>* Total Revenue: EUR 40 MILLION<br>* 250 employees               | An entity is consolidated when it is considered to be under<br>"control"<br>Having "control" is defined as having the power to control<br>the assets of an entity and being exposed to the results of<br>that entity.<br>In identifying subsidiaries and associates, the existence of<br>currently exercisable potential voting rights is taken into<br>consideration.<br>SPVs are considered "controlled entities" when the<br>investor is exposed to the variability of the SPV's results; a<br>specific threshold of relevance is not provided. |
| As   | sets   |
| Acquired inte  | angible assets   |
| All intangible fixed assets are amortised and some have<br>a maximum useful life of five years. Start-up costs (i.e.<br>training), and the cost of issuing shares can be capitalised,<br>with certain restrictions. Advertising costs may be not<br>capitalised. Goodwill arising from a business combination<br>is amortised over its useful life. The amortisation period<br>cannot be longer than 10 years by law (Italian GAAPs<br>allow this period to be extended to a maximum of 20 years<br>in certain cases). Revaluations are not permitted unless<br>authorised by special laws.                            | If the criteria for capitalisation are satisfied, intangible<br>assets must be amortised over their estimated useful life.<br>The cost of issuing shares is recognised as a deduction<br>from equity.<br>Goodwill arising from a business combination and<br>intangible assets with an indefinite useful life are not<br>amortised but subject to an impairment test at least once<br>a year.<br>Revaluations are only possible in very few cases.   |
| Internally generate  | ed intangible assets   |
| Research costs may not be capitalised. Similar to<br>IFRS, except that there is the option of capitalising and<br>amortising development costs if the conditions are<br>satisfied.   | Research costs are charged when incurred. Development costs are capitalised and amortised when rigorous criteria are satisfied.  |
| Property, plant  | and equipment  |
| These must be stated at their historical cost.<br>Revaluations are not permitted unless authorised by<br>special laws.   | These are measured using either the cost model or the<br>revaluation model. When the revaluation model is used,<br>the entire category of assets has to be revaluated with<br>sufficient regularity.   |

| Leases (as lessee)   |  |  |  |
|--|--|--|--|
| All leases are accounted for in the financial statements<br>as operating leases. Disclosures are required by law for<br>financial leases.  | Financial leases are accounted for in the financial statements on the basis of substance rather than form.   |  |  |
|  | t properties   |  |  |
| These must be stated at cost and depreciate over their useful life. Fair value is not permitted.   | These must be stated at their depreciated cost or at fair value. If fair value is used, variations are recognised in the profit or loss.   |  |  |
|  |  |  |  |
| Similar to IFRS, although the FIFO, LIFO and Weighted Average Cost methods are allowed.  | Stated at the lower of cost and net realisable value. The cost is calculated using the FIFO or Weighted Average Cost Method. The LIFO method is not admitted.  |  |  |
| Financial assets (measur   | ement and derecognition)   |  |  |
| Long-term investments are accounted for at the cost of<br>acquisition. When this cost is durably impaired, they are<br>accounted for at the lower value.<br>Short-term investments are accounted for at the cost of<br>acquisition. They are valued at the lower of the cost of<br>acquisition and the market value.<br>Loans and receivables with a reduced and favourable<br>interest rate are accounted for at their amortised cost.<br>No guidance for derecognition. Generally based on the loss<br>of legal ownership. | <ul> <li>Measurement of financial assets depends on their classification:</li> <li>at their amortised cost (held-to-maturity assets, loans and receivables)</li> <li>at their fair value through equity (financial assets available for sale)</li> <li>at their fair value through profit or loss (financial assets not included in the above categories)</li> <li>The derecognition of financial assets is mainly based on the transfer of risk and rewards.</li> </ul> |  |  |
| Hedging deriva   |  |  |  |
| Specific guidance is provided by OIC document no. 32 on<br>the definition, valuation of hedging derivatives and the<br>information required in the statutory financial statements.<br>Similarly to under IFRS, all derivative instruments are<br>measured at their fair value.<br>"Fair value hedges" have different representation criteria<br>to "cash flow hedges".   |  |  |  |
| LIABILITIES  | AND EQUITY   |  |  |
| Financial liabilities and equi   | ty instruments (classification)  |  |  |
| Classification is based on the legal form of the financial<br>instruments.<br>Preference shares are always included in equity.<br>Convertible debt is always recognised as a financial<br>liability.<br>Similarly to under IFRS, purchased own shares are<br>recognised as a deduction from equity.  | Classification depends on the substance of the issuer's<br>obligations.<br>Mandatorily redeemable preference shares are classified<br>as financial liabilities.<br>Proceeds received as a result of issuing convertible debt<br>are allocated between equity and financial liabilities.<br>Purchased own shares are recognised as a deduction from<br>equity.  |  |  |
|  |  |  |  |
| A restructuring provision is recognised at the moment of the board of directors' resolution.   | A restructuring provision must be made if a detailed plan<br>has been announced or if the implementation of a plan has<br>actually started.  |  |  |

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| INCOME STATEMENTS   |  |  |
|---|--|--|
|   |  |  |
| OIC document no. 12 provides guidelines on revenue<br>recognition.<br>Revenues are generally recognised when ownership is<br>transferred or when revenue is legally enforceable.<br>Based on several criteria, which require the recogniti<br>revenue when risks and rewards have been transferred<br>the revenue can be measured reliably. |  |  |
| Employee benefits – pension costs (defined benefit plans)   |  |  |
| There is no binding guidance on pension costs. The actuarial calculation may apply in calculating the amount to be set aside for severance pay (i.e. TFR – <i>trattamento di fine rapporto</i> ) when the amount and the long term period are relevant.   | The amount to be set aside for a defined benefit plan is estimated using an actuarial calculation (projected unit credit method) |  |

# 4.8 Due dates for filing the year-end accounts and tax returns and for making tax payments

#### 4.8.1 Year-end accounts

|    | Task  | Description   | Deadline  |
|----|---|---|---|
| 1. | Approval of the annual financial statements | The shareholders approve the<br>year-end accounts (including notes)<br>by adopting a specific resolution<br>during a general meeting convened<br>in accordance with the company's<br>articles of association. | Within 120 days of the tax year-end<br>(180 days in special circumstances). |
| 2. | Filing of the year-end accounts             | The annual financial statements<br>(including the notes) and the<br>minutes of the shareholders'<br>meeting must be filed in electronic<br>format at the local Trade Register.                                | Within 30 days of the shareholders' approval.                               |
| 3. | Updating of the inventory ledger            | The inventory ledger must be updated<br>by adding details of the assets<br>and liabilities shown in the annual<br>financial statements.   | Within three months of the annual income tax return filing date.            |

#### 4.8.2 Tax returns and tax payments

|     | Task   | Description  | Deadline   |
|-----|--|--|--|
| 1.  | Filing of the annual VAT return for the previous calendar year.  | The VAT return for the previous calendar year must be filed.<br>No late filings are allowed.   | 28 February 2017<br>for financial year<br>2016, 30 April<br>for subsequent<br>financial years. |
| 2.  | Filing of certificates of income subject to withholding tax  | The certificates must be filed electronically and sent by recorded delivery letter to every local payee (e.g. agents, professionals, employees) and non-resident entity that has received payments of royalties, interest or dividends.  | 7 March  |
| 3.  | Payment of the annual duty on accounting records.  | A duty of EUR 309.87 must be paid if the quota/share capital<br>is lower than EUR 516,456.90, otherwise the duty is EUR<br>516.46.   | 16 March   |
| 4.  | Payment of any remaining VAT<br>not paid during the previous<br>calendar year by the monthly<br>due dates.   | The difference between output and input VAT is payable<br>on the 16th of each subsequent month. Late payments are<br>subject to fines.   | 16 March   |
| 5.  | Filing of the annual<br>compulsory communication<br>of relevant transactions<br>for Italian VAT purposes<br>including the annual black-list<br>communication | The annual compulsory communication of relevant transactions for Italian VAT purposes including the annual black-list communication must be filed electronically using the " <i>Modello Polivalente</i> " form.  | 10 April 2017<br>(only for the 2016<br>financial year)   |
| 6.  | Payment of the balance of<br>income taxes (IRES + IRAP)<br>for the tax year ending 31<br>December.   | The income taxes payable are net of the advances due by the 20th day of the sixth month and by the end of the 11th month of the previous tax year.   | 30 June  |
| 7.  | Payment of the annual<br>registration duty at the Trade<br>Register.   | Payment is due on the same date as payment of the<br>balance of income taxes; the amount is decided by the<br>Chamber of Commerce and published in advance.  | 16 June  |
| 8.  | Filing of the annual withholding tax return (770 tax return).  | The 770 tax return must be filed electronically.   | 31 July  |
| 9.  | Filing of the income tax return<br>for the tax year ending 31<br>December ( <i>Unico tax return</i> ).   | The Unico tax return must be filed electronically.   | 30 September   |
| 10. | Payment of the advance VAT due for December.   | When applicable, and based on the historical method,<br>the advance VAT due equals 88 percent of the VAT paid in<br>December of the previous year  | 27 December  |
| 11. | Quarterly VAT communication<br>- transmission of the data on<br>sale and purchase invoices.  | The data must be filed electronically using special<br>software. Data on periodic VAT payments must be<br>included.<br>It must be sent quarterly by the end of the second month<br>following the end of each quarter (eg Q1 by 31/05, Q2 by<br>31/07, etc).<br>In the first year of application, 2017, the filing date for<br>both Q1 and Q2 data is 31/07/2017. | Quarterly  |

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## 4.9 Failure to keep accounting books and records properly

The failure to keep accounting records is punishable by fines ranging, for the period up to 31 December 2016, from EUR 1,032.00 to EUR 7,746.00 and, as of 1 January 2017, from EUR 1,000.00 to EUR 8,000.00. Fines are doubled if, in any tax year, unpaid corporate taxes or VAT amount to more than EUR 51,645.69 for tax periods up to 31 December 2016, and more than EUR 50,000.00 from 1 January 2017.

If the company fails to keep accounting books and records for the purpose of concealing profits or turnover, the legal representative is liable to criminal prosecution.

Upon the incorporation of a company, the tax authorities must be informed of where the accounting books and records are kept and may be accessed during tax inspections. Any subsequent changes must also be notified accordingly.

Bookkeeping abroad is allowed on the condition that all mandatory accounting books and records can be printed out promptly when necessary, i.e. during tax inspections. The original documentation must, however, be stored in Italy until such time as the law allows for an optical storage system.



## 5. Taxation of business income

## 5.1 Corporations

#### BASIC TAX FACTS

| Corporate tax rate                  | 24% (IRES)+<br>3.9% (IRAP)    |
|-------------------------------------|-------------------------------|
| Thin cap rule on interest deduction | No (but certain limits apply) |

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| Rules on dormant companies   | Yes  |
|--|--|
| Patent Box regime  | Yes  |
| Loss relief (carryforward/carryback)   | Carryforward   |
| Capital gains tax rate   | 13.95%/26%/0   |
| Participation exemption  | Yes (95% exemption)  |
| Withholding tax rate on dividends paid to non-residents (pre-<br>treaty relief)                        | 26%/1.2%/0%  |
| Withholding tax rate on interest paid to non-residents (pre-<br>treaty relief)                         | 26%/12.5%/5%/0%  |
| Withholding tax rate on royalties paid to non-residents (pre-<br>treaty relief)                        | 22.5%/30%/0%   |
| Approximate number of countries with which Italy has a tax treaty                                      | 94   |
| Double taxation relief for dividend income from controlled<br>subsidiaries (tax with credit/exemption) | Exemption (95%)  |
| Double taxation relief on income derived from a foreign PE (foreign tax credit/exemption)              | Foreign tax credit;<br>exemption (optional)<br>under certain<br>conditions |
| Tax group  | Yes  |
| Double taxation relief   | Yes (foreign tax credit)   |
| General anti-avoidance rule  | Yes  |
| CFC rule   | Yes  |

#### 5.1.1 Tax residence

A company or entity is tax resident in Italy if its registered office, place of management or main business is in Italy for more than half of the tax year.

Resident companies are taxed on their worldwide income, while nonresidents are only taxed on their Italian-source income.

#### 5.1.2 Rates

The IRES rate is 24 percent. For banks and other financial institutions, it is 27.5 percent.

The standard IRAP rate is 3.9 percent but Italian regions may increase or decrease the standard rate by up to 0.92 percent. The compound tax rate is therefore approximately 27.9 percent, whilst the effective rate may be very different.

The IRAP base is normally different from the IRES base.

#### 5.1.3 Calculation of taxable income

#### For IRES purposes

The taxable income is calculated on the basis of the P&L account, drawn up according to Italian GAAP or IAS/IFRS and adjusted in accordance with tax law and regulations. The accruals method is generally used, with certain exceptions (e.g. dividends and directors' fees are taxed upon receipt).

To qualify for tax purposes, expenses must be (i) certain – in the sense that they certainly exist, (ii) objectively quantifiable at the end of the tax year, and (iii) recorded in the company's accounts. In general, costs and expenses recorded in the P&L account can be deducted for tax purposes. However, the following are never deductible:

- generic risk provisions or provisions not specified in tax law (such as that for inventory obsolescence);
- costs/expenses related to prior years (known as 'sopravvenienze passive').

For IAS/IFRS adopters (e.g. banks and listed companies), the IAS/ IFRS criteria for the definition, accrual and classification of income and costs also apply for corporate income tax purposes and prevail over any provisions contained in the ITC.

#### For IRAP purposes

The taxable income is calculated exclusively on the basis of the P&L account, with certain adjustments. For instance, bad debts and interest expense (including interest on lease payments) are generally non-deductible.

The labour costs of employees with a permanent contract are fully deductible for IRAP purposes. The labour costs of temporary employees are partially deductible (70 percent of the costs) if certain conditions are met.

IAS adopters must base their calculation on the corresponding items of their IAS/IFRS income statement.

IRAP itself is not an allowed expense; however, for IRES purposes, since the tax year in progress on 31 December 2008, 10 percent of

IRAP payments have been deductible. This amount should, in principle, correspond to the IRAP paid on interest. Furthermore, IRAP paid on non-deductible labour costs – if there are any – is deductible from the IRES taxable base.

Special rules apply to banks and insurance companies.

### 5.1.4 Tax treatment of (inbound) dividends and capital gains/losses

#### Dividends

Ninety-five percent of domestic dividends are exempt from IRES. For IAS/IFRS-adopters, however, dividends received on shares that are held-for-trading are fully taxable.

Domestic dividends and capital gains on shares are not included in the IRAP base.

Ninety-five percent of foreign dividends are also exempt from IRES, if the distributor is (i) not resident in a black-list jurisdiction and (ii) not allowed to deduct the dividend distribution<sup>1</sup>.

Until 2015, 100 percent of the dividends received by a resident taxpayer directly from an affiliate located or operating in a CFC black-list country (as of 2016, these are countries whose ordinary or special tax regimes grant a nominal level of taxation of less than half the level of taxation in Italy - see the below section headed 'CFC rule') or indirectly through, for example, Italian or foreign non-black-list affiliates, were subject to IRES in Italy. Exceptions were made only for the following.

- The portion of the dividend corresponding to the CFC income previously allocated and taxed to the Italian shareholder, under the CFC rule<sup>2</sup>.
- b. Whole dividends taxed at an acceptable level before being received by the Italian shareholder (e.g. at least 75 percent of dividends taxed to an intermediate white-list holding company – the 'safe-harbour rule' or 'subject-to-tax rule'). It was possible to submit an application for a ruling on this.

The above rule has been partially amended so that – unless the two exceptions apply – black-list dividends paid from 2015 are 100 percent subject to tax if received directly from an affiliate located or operating in a CFC black-list country or indirectly through intermediate companies that are under the Italian shareholder's control.

Moreover, black-list dividends must now be reported separately in the

<sup>1</sup> Article 26 of the European Law n. 122/2016 provides that, starting from 2016, dividends paid by an EU P/S qualifying subsidiary to its Italian parent are 95% exempt up to the amount that is un-deductible upon the subsidiary. 2 See the section headed 'CFC rules'.

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income tax return if no advance tax ruling is required in order to benefit from the safe-harbour rule (or the outcome of the ruling is unfavourable). Penalties apply if black-list dividends are not reported separately in the tax return.

#### Capital gains on the transfer of shares

Capital gains on the transfer – by a non-resident company with no permanent establishment in Italy – of shares in listed Italian companies are taxable in Italy, even if the shares are not held through an Italian bank.

- If the shares sold during a 12-month period are not listed and represent more than 20 percent of the voting rights or 25 percent of the stated capital ('qualifying' shares), only 58.14 percent<sup>3</sup> of the gain is included in taxable income and taxed at the general 24 percent rate. The same percentage of capital losses is deductible. The taxpayer must report the capital gains and losses in its income tax return.
- If a resident company is not listed and the shares sold during a 12-month period do not represent more than 20 percent of the voting rights or 25 percent of the stated capital ('non-qualifying' shares), the capital gains are subject to a 26 percent final substitute tax (20 percent until 30 June 2014). Residents of white-list countries<sup>4</sup> are exempt from taxation on these capital gains.
- If a resident company is listed and the amount of shares sold during a 12-month period does not represent more than 2 percent of the voting rights or 5 percent of the stated capital ('non-qualifying' shares), the capital gain is not regarded as Italian-source income. By contrast, if the amount of shares sold during a 12-month period represents more than 2 percent of the voting rights or 5 percent of the stated capital ('qualifying' shares), 58.14 percent of the capital gain is included in taxable income and taxed at the general 24 percent rate.
- If a tax treaty applies, capital gains are usually taxable only in the seller's country of residence.

<sup>3</sup> This percentage rate should be confirmed by an implementing Decree, yet to be published.

<sup>4</sup> The White List is a list of countries that allow an adequate exchange of information with Italy, This list currently includes: Albania, Alderney, Algeria, Anguilla, Argentina, Armenia, Aruba, Australia, Austria, Azerbaijan, Bangladesh, Belarus, Belgium, Belize, Bermuda, Bosnia and Herzegovina, Brazil, British Virgin Islands, Bulgaria, Cameroon, Canada, Cayman Islands, China (People's Rep.), Colombia, Congo (Rep.), Cook Islands, Costa Rica, Croatia, Cura ao, Cyprus, Czech Republic, Denmark, Ecuador, Egypt, Estonia, Ethiopia, Faroe Islands, Finland, France, Georgia, Germany, Ghana, Gibraltar, Greece, Greenland, Guernsey, Herm, Hong Kong, Hungary, Iceland, India, Indonesia, Ireland, Isle of Man, Israel, Ivory Coast, Japan, Jersey, Jordan, Kazakhstan, Korea (Rep.), Kuwait, Kyrgyzstan, Latvia, Lebanon, Liechtenstein, Lithuania, Luxembourg, Macedonia, Malaysia, Malta, Mauritius, Mexico, Moldova, Montenegro, Montserrat, Morocco, Mozambique, Netherlands, New Zealand, Nigeria, Norway, Oman, Pakistan, Philippines, Poland, Portugal, Qatar, Romania, Russia, San Marino, Saudi Arabia, Senegal, Serbia, Seychelles, Singapore, Slovak Republic, Slovenia, South Africa, Spain, Sri Lanka, St. Maarten, Sweden, Switzerland, Syria, Taiwan, Tajikistan, Tanzania, Thailand, Trinidad and Tobago, Tunisia, Turkey, Turkmenistan, Turks and Caicos Islands, Uganda, Ukraine, United Arab Emirates, United Kingdom, United States, Uzbekistan, Venezuela, Vietnam and Zambia.

#### These rules are summarised in the following table.

#### Capital gains realised by a non-resident (corporate) shareholder with no permanent establishment in Italy from the sale of shares in Italian companies

| Shareholding |   | Taxable<br>gain | Tax rate   |
|--------------|---|-----------------|--|
|              | >20% voting rights or >25% capital (qualifying)                           | 58.14%          | 24%  |
| Non-listed   | 20% or less of voting rights; 25% or less of capital (non-<br>qualifying) | 100%            | 26% (final WHT);<br>zero if the investor<br>is white-list. |
| listed       | >2% voting rights or >5% of capital (qualifying)                          | 58.14%          | 24%  |
| Listed       | 2% or less of voting rights or 5% or less of capital (non-<br>qualifying) | -               | -  |

Under the Participation Exemption regime, 95 percent of capital gains earned by a resident company from the transfer of shares or quotas, equivalent financial instruments, and equity interests in partnerships are tax-exempt if the following requirements are met.

- The seller has held the shares uninterruptedly for 12 months before their transfer (FIFO is used in the case of shares issued by the same company and purchased at different times).
- The shares are booked under fixed assets in the first financial statements approved after their purchase.
- The shares are in a company which, in the three years before their transfer, engaged in actual business and was resident in a "whitelist" country (or an advance ruling is obtained, confirming that the company directly produced most of its taxable income in a white-list country).

If these requirements are met, 95 per cent of capital losses earned from the transfer of shares are not deductible.

If these requirements are not met, IRES (no IRAP) is due upfront and cannot be paid in instalments.

Write-offs, losses and step-ups in the tax basis of shares are not normally tax-relevant (occasionally, however, temporary rules have been issued, allowing step-ups against payment of substitute tax).

#### Capital gains on business assets

Capital gains on the sale of business assets may be taxed upfront or over a maximum of five years, starting from the year in which the gain is realised (in this second case the assets must have been held for at least three years before disposal). These gains are subject to both IRES and IRAP; however, when realised on the transfer of a business concern, or a branch of business, they are only subject to IRES and are exempt from IRAP.

#### 5.1.5 Deductions

A number of deductible business expenses are specified in tax law and described in the following sections. The items (by no means an exhaustive list) are deductible for both IRES and IRAP purposes, unless otherwise stated.

#### Depreciation of tangible assets

The depreciation of income-producing assets is based on their purchase or manufacturing cost, which may include interest on funds borrowed to purchase the assets. That interest must be capitalised until the asset goes into use.

Depreciation should start from the date an asset is first used. It should be charged on a straight-line basis over the estimated useful life of the asset, which can be determined using the Ministry of Finance tables provided for each sector of industry and each category of assets.

In the first year of use, the ordinary depreciation rate is halved.

If the purchase cost of the asset is not higher than EUR 516.00, it may be fully deducted in the year of purchase.

#### Extra depreciation:

The extra depreciation regime provided for by article 1(91) of Law no. 208/2015 has been extended by one year. Therefore, for business income and self-employment income tax purposes and in exclusive reference to the calculation of depreciation rates and financial lease payments, the depreciation of investments in new tangible operating assets up to 31 December 2017 is increased by 40 percent. The benefit also applies to investments made by 30 June 2018, as long as the order is accepted by the supplier and at least 20 percent of the cost is paid before the end of 2017. The benefit is only relevant for income tax and not for IRAP purposes. For lease payments, the benefit only applies to the principal amount, which can be increased by the cost of redemption. Unlike in the previous version, however, vehicles and the other means of transport indicated in letters b) and b-bis) of paragraph 1 of article 164 of the Italian Income Tax Code ('vehicles for public use') are excluded. Motor vehicles used solely as operating assets in a company's activities still benefit. The benefit only applies to depreciation costs, and therefore has no impact on capital gains or losses if the asset is disposed of, or on the parameters for determining maintenance and repair cost limitations.

The benefit does not apply to investments in: real estate assets; other tangible assets for which the Ministerial Decree of 1988 provides a depreciation rate lower than 6.5 percent; or the assets indicated in Appendix 3 to the 2016 Stability Law (e.g. pipelines).

#### Hyper depreciation:

The 'hyper depreciation' regime has been introduced for certain highly technological operating assets identified in the Budget Law for 2017. The depreciation cost of these assets has been increased by the following percentages:

- a. 150 percent for investments in the new operating assets listed in Appendix A to the Budget Law;
- b. 40 percent for investments in the intangible assets (e.g. software) listed in Appendix B to the Budget Law and used to operate the assets under a).

To obtain the benefit, the legal representative of the Company must provide a self-declaration issued pursuant to Presidential Decree 445 of 28 December 2000, or if the purchase cost of the asset exceeds EUR 500,000, a technical appraisal to confirm that the asset meets the indicated requirements.

The above benefit should not be considered when determining the advance payments due for the tax year in progress on 31 December 2017 or for the following year.

#### Amortisation of intangible assets

Patents and know-how: up to 50 percent of the cost of the asset can be deducted in each tax year, i.e. the minimum amortisation period is two years.

*Goodwill and trademarks*: up to 5.55 percent of the cost of the asset can be deducted in each tax year, i.e. the minimum amortisation period is 18 years. The amortisation of goodwill and trademarks is deductible regardless of how they are recorded in the company's accounts; therefore, it can also be deducted by IAS/IFRS adopters, whose goodwill and trademarks should be tested for impairment rather than amortised.

*Licences and other rights*: amortisation is deductible on a straight-line basis over the useful life of the asset, as determined by the underlying contract or by law.

#### Repairs and maintenance

Ordinary repair and maintenance costs are deductible to the extent of five percent of the gross value of the depreciable tangible assets at the beginning of the tax year. Any remaining costs may be deducted over the following five tax years.

#### Entertainment expenses

Entertainment expenses are deductible if they (i) meet specific criteria that differentiate them from advertising and marketing costs, and (ii) are business-related, reasonable and properly documented.

Free gifts costing not more than EUR 50.00 each are immediately and fully deductible.

Special provisions apply to pharmaceutical companies, e.g. partial deduction of conference costs, and no deduction of costs of goods and services offered directly or indirectly to doctors, vets or pharmacists in order to promote sales of drugs or pharmaceutical goods.

#### Interest expense

Net interest expense (interest expense exceeding interest income) can be deducted to the extent of 30 percent of EBITDA (gross operating income). EBITDA is the difference between the value of production (item A of the P&L account) and the cost of production (item B of the P&L account), excluding depreciation, amortisation, and finance lease payments for business assets. IAS adopters must base their calculation on the corresponding items of their IAS/IFRS income statement. Any portion of the interest expense that exceeds 30 percent of EBITDA may be carried forward indefinitely and deducted in subsequent tax years to the extent that the net interest expense accrued in those subsequent years is less than 30 percent of EBITDA. If, in a given tax year, the 30 percent of EBITDA is higher than the net interest expense, the surplus may be carried forward indefinitely and used to increase the EBITDA available in subsequent years.

Within a domestic tax group, a company may offset the portion of its interest expense (accrued since it joined the tax group) that exceeds 30 percent of its EBITDA against the 30 percent of EBITDA that another company in the tax group has not used to deduct its own interest expense. Since 2016, the 'virtual inclusion in the tax group' of foreign affiliates for the purpose of interest offsetting has no longer been allowed.

Dividends paid by foreign companies to an Italian company are included in the EBITDA.

Special rules apply for banks, financial institutions and insurance companies.

#### Research and development expenses

R&D expenses are deductible in the tax year in which they are incurred or, at the taxpayer's choice, in equal instalments in the same year and over the next four years. In the second case, the taxpayer cannot reverse its decision.

#### Inventory

For income tax purposes, inventory can be valued using any reasonable costing method, such as FIFO, LIFO or weighted average cost; however, it cannot be valued at less than its LIFO value. A write-down of inventory to its market value is deductible only when the average unit cost of the goods in the inventory is higher than their average market value during the last month of the tax year. Any other write-down is generally deductible only when the loss is realised, i.e. when the goods have been sold or destroyed, in which case formal procedures must be followed. Work in progress and finished goods should be valued at production cost, inclusive of production overheads. Special rules apply to the valuation of long-term contracts.

#### Provision for bad debts

A provision for bad debts is allowed each year, to the extent of 0.5 percent of the face value (or acquisition cost) of the receivable that is not covered by any form of guarantee. However, if the total provision for bad debts exceeds 5 percent of the aggregate face value (or acquisition cost) of the trade receivables shown in the annual financial statements, deductions for provisions are no longer allowed. Provisions are deductible for IRES purposes only. Special rules apply to banks, financial institutions and insurance companies.

The partial or total write-off of a receivable is allowed only if insolvency proceedings have started or when it can be proved that no amount is recoverable.

Credit losses are deductible in either of the following cases.

- I. If they are substantiated by certain and precise details.
- II. If the debtor is going through insolvency proceedings or has an agreed restructuring plan<sup>5</sup>.

Details are certain and precise when, for example, the account receivable has been written off or derecognised or, if the face value of the receivable is not higher than EUR 2,500 (or EUR 5,000 in the case of companies with turnover of EUR 100 million or more), when the debt has been overdue for at least six months.

Credit losses can also be deducted when substantiated by foreign insolvency proceedings equivalent to Italian ones. Whether the customers are going through Italian insolvency proceedings or equivalent foreign proceedings, if the face value of the debt is not higher than EUR 2,500 (or EUR 5,000 in the case of companies with turnover of EUR 100 million or more) and the debt has been overdue for at least six months, the rule on when they can be deducted is the same: credit

<sup>5</sup> The restructuring plan indicated in article 182-bis of the Italian Bankruptcy Law.

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losses are deductible in the tax year in which they are recognised in the accounts, even if this is after the year in which the debtor goes into insolvency or the credit losses are substantiated by certain and precise details. However, from the tax year in which they must be derecognised in accordance with the relevant accounting standards, such credit losses can no longer be deducted.

In 2015, new rules on the deduction of bad loans by banks and other financial institutions came into force. Such institutions may now deduct 100 percent of all kinds of write-offs and write-downs of qualifying loans in the tax year in which they are booked for statutory accounting purposes.

#### Tax losses

For IRES purposes only, companies may carry forward tax losses indefinitely and use them to offset up to 80 percent of the taxable income of any subsequent year. However, the 80 percent limit does not apply to tax losses incurred in the first 3 years of business, which can be offset against 100 percent of the taxable income of any future year until they are used up.

Carry forward is not allowed when both of the following apply.

- The majority of the shares carrying voting rights at ordinary shareholders' meetings are, even temporarily, transferred to third parties.
- The company's main activity is no longer the actual business that it pursued in the tax years when it incurred the losses (this change is significant if it occurs in the tax year of the transfer or the two previous or subsequent years).

There may also be limits on loss carryforwards when a company has been involved in a merger or demerger. However, there are safe-harbour rules (a business vitality test).

There is no limit on the tax losses that can be transferred to the parent of a tax group if they originate during the consolidation period. The parent can carry forward group losses in accordance with the general rules (the losses can be used to offset up to 80 percent of the taxable income of each year, or up to 100 percent if incurred in the first three years of business).

#### 5.1.6 Dormant companies

Italian companies, partnerships and permanent establishments of nonresident enterprises are treated as dormant in certain circumstances (i.e. if their taxable income falls below levels commensurate with the nature and book value of their assets – failure to pass the 'vitality test'). In such cases, a minimum level of taxable income is deemed to be realised for IRES and IRAP purposes. Dormant companies are subject to a 10.5 percent IRES surtax (making the nominal rate 34.5 percent).

Safe-harbour rules apply, inter alia, to the following:

- companies that, even indirectly, control or are controlled by publicly traded companies;
- companies in their first year of business;
- companies going through bankruptcy proceedings;
- companies that have obtained an advance tax ruling.

Dormant companies may also rebut the minimum taxable income presumption by giving evidence of circumstances that have prevented them from meeting the vitality test. To this end, a company can either obtain a positive ruling from the tax authorities confirming the existence of such circumstances, or give separate indication of the existence of such circumstances in its annual tax return.

Dormant companies may carry forward their tax losses and offset them against any portion of taxable income that exceeds the minimum level.

A company is also deemed to be dormant from the sixth tax year if it has reported one of the following:

- I. Tax losses for five consecutive tax years.
- II. Tax losses in four tax years and taxable income lower than the minimum deemed income of dormant companies in the fifth year.

#### 5.1.7 Incentives

#### Patent Box

From the tax year following that in progress on 31 December 2014, entrepreneurs resident in Italy, or entities with a PE in Italy resident in countries that have signed a double tax treaty and exchange information with Italy, may opt for the Patent Box regime if they carry out R&D activities.

Under the regime, a certain percentage of qualifying income is excluded from the tax base. Qualifying income is that deriving from the licensing or direct use of eligible IP (software protected by copyright, patents, trademarks, designs, models, processes, secret formulas and industrial, commercial or scientific knowledge). The percentage of qualifying income that is not included in the IRES or IRAP base is 30 percent for 2015, 40 percent for 2016, and 50 percent from 2017 (for calendar-year taxpayers). Once it has been opted for, the arrangement is irrevocable and remains in place for 5 years. It can be renewed.

When income is attributable to direct use of intangibles by their owner, its amount has to be agreed with the tax authorities through the international tax ruling procedure.

The eligible portion of the tax base is given by the ratio of the R&D costs incurred in maintaining and developing the intangible asset to the total costs of producing that asset.

This computation method is compliant with the OECD 'nexus approach'.

Gains from the transfer of qualifying assets are excluded from the tax base, provided that 90 percent or more of the consideration is reinvested in maintenance or development of other qualifying intangible assets before the end of the second tax year following that of the asset transfer.

A decree issued by the Ministry for Economic Development on 30 July 2015, in collaboration with the Ministry of Economy and Finance, contains implementation measures that clarify the main technical aspects, e.g. calculation of the eligible tax base.

The decree states, inter alia, that the IP income covered by the regime is determined on the basis of OECD international standards, referring in particular to the 'OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations'.

#### R&D tax credit

The Budget Law which was approved in 2016 modified the R&D tax credit regime. An enterprise now qualifies for a tax credit if:

- I. it invests at least EUR 30,000 per year in certain forms of R&D, and
- II. its total R&D spending in a given year exceeds the average amount spent on corresponding forms of R&D over the three tax years preceding that in progress on 31 December 2016 (i.e. 2013, 2014 and 2015 for calendar-year taxpayers).

The tax credit is 50 percent of the difference in spending and is capped at EUR 20 million per year for each beneficiary.

#### Allowance for corporate equity

Italian resident companies (and permanent establishments of nonresident entities) can benefit from ACE, which is calculated by multiplying a certain amount of equity (the portion by which equity – as defined in the relevant rules – has increased since 31 December 2010 by a nominal rate of interest. The rates are 4 percent for 2014, 4.5 percent for 2015 and 4.75 percent for 2016. The rate drops to 2.3 percent for 2017 and 2.7 percent for 2018.

The equity increases that qualify for ACE purposes include those resulting from (i) cash contributions, (ii) waivers of amounts owed by a company to its shareholders, and (iii) undistributed profits set aside to freely disposable reserves. The equity increases must be net of decreases resulting from distributions or assignments of shares to shareholders. The equity increase is reduced by certain group transactions, and specific anti-tax avoidance rules apply to

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equity injections made by non-resident shareholders. General anti-tax avoidance rules also apply.

The allowance is deducted from the company's net taxable income but cannot result in a tax loss. Should the allowance be higher than the year end taxable income, the difference can be carried forward to offset the taxable income of future years.

#### 5.1.8 Withholding taxes

#### Dividends paid to non-residents

Dividends paid to non-resident shareholders are generally subject to a 26 percent WHT. A partial refund of up to 11/26 of the WHT can be claimed by recipients who are able to prove – by presenting documentary evidence issued by their foreign tax authority – that a final tax has been paid on the same dividends. There is also a 26 percent WHT on savings shares (but no 11/26 tax credit refund). The WHT rate is 11 percent on dividends paid to EU and EEA white-list pension funds (with no 11/26 tax credit refund).

The above rates may be reduced under tax treaties.

In accordance with the Parent-Subsidiary Directive, no WHT is levied on dividends paid to a qualifying EU parent company that has owned at least 10 percent of the Italian subsidiary's equity for an uninterrupted period of at least one year before payment of the dividends (a qualifying company is one that has one of the legal forms covered by the Parent-Subsidiary Directive, is resident in an EU Member State and is not exempt from income taxes). General anti-avoidance rule applies.

The beneficial owner must submit a form to the payer (the withholding tax agent) by the payment date of the profits in order to benefit from the exemption (the form includes a certificate of residence signed by the foreign tax authorities and an attestation by the recipient that the minimum holding period has been respected).

Should the Parent-Subsidiary Directive be inapplicable, dividends paid to companies or other entities that are resident and paying CIT in an EU or an EEA white-list (i.e. Norway or Iceland or Liechtenstein) country may be subject to a reduced 1.2 percent domestic WHT (the same level of taxation applied to dividends received by domestic parent companies).

Under article 15 of the Savings Agreement of 26 October 2004 between the European Union and Switzerland, Italy must exempt dividend payments to companies resident in Switzerland under essentially the same conditions as those laid down in the EC Parent-Subsidiary Directive (before the amendments effective from 1 January 2005). The conditions are listed below.

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- The parent must have directly held at least 25 percent of equity of the subsidiary for at least two years.
- One company must be resident for tax purposes in Italy and the other company must be resident for tax purposes in Switzerland.
- Under any double tax agreements with any third states, neither company must be resident for tax purposes in that third state.
- Both companies must be fully subject to corporate income tax, without benefitting from exemptions.
- Each company must be a corporation.

#### Interest and royalties paid to non-residents

#### Interest

In general, there is a 26 percent WHT on interest payments. This rate may be reduced under tax treaties. There are also certain domestic lower rates or exemptions (see below). For instance, interest from Italian treasury bonds and similar instruments is taxed at a lower rate of 12.5 percent. Moreover, an exemption is available if the requirements of the Interest and Royalties Directive are met (see below under the section on "Withholding tax exemption under Interest and Royalties Directive").

#### Interest paid by an Italian company to an EU affiliate

A lower 5 percent WHT is levied on interest paid by an Italian company to an affiliate established in another EU Member State if:

- all the exemption requirements established by the Interest & Royalties Directive (see below) are met, apart from the payee's beneficial owner status;
- II. the non-resident affiliate issues bonds that are listed on a regulated market of an EU or EEA white-list country;
- III. the interest payments to the EU company service interest payments to the bondholders;
- IV. the bonds issued by the EU company are guaranteed by the Italian company or another group company (e.g. the parent).

### Withholding tax exemption on interest paid on qualifying bonds to a foreign white-list taxpayer

Interest and similar proceeds (e.g. issue discounts) are exempt if both the following conditions are satisfied.

a. The non-resident payee is (i) a foreign central bank or body that invests the public reserves of its country, or (ii) resident in a whitelist jurisdiction, whether or not subject to tax (these residents may include institutional investors such as investment funds). b. Interest accrues on, inter alia, the following assets: (i) Italian and other white-list treasury bonds; (ii) bonds, bond-like securities and commercial papers issued by Italian banks or by Italian companies whose shares are traded on regulated markets or the multilateral trading facilities of a white-list EEA country; (iii) notes issued by securitization vehicles (as defined by Law no. 130/1999). In certain cases, interest on bonds, bond-like securities and commercial papers issued by non-listed entities can also benefit from the tax exemption.

In order to benefit from the exemption, the non-resident beneficial owner must deposit the bonds with a resident bank or other authorised intermediary and file a special form.

# WHT exemption on interest on cross-border loans

The exemption also applies to interest on cross-border loans if all of the following apply.

- I. The loan is medium- or long-term.
- II. The borrower is a resident enterprise.
- III. The lender is a bank or insurance company established in an EU Member State or an institutional investor set up and subject to supervision in a country on the White List (e.g. an investment fund).

# Royalties

Generally, a 30 percent final WHT is levied on 75 percent of the gross royalties (i.e. 22.5 percent) arising from IP and paid by a resident taxpayer (including a permanent establishment in Italy of a non-resident) to a non-resident taxpayer.

A 30 percent WHT is also levied on the full amount of royalties (or 'rent') represented by payments for the use of, or the right to use, industrial, commercial or scientific equipment located In Italy.

There is no WHT on payments to Italian permanent establishments of non-resident entities.

The WHT may be reduced or eliminated under tax treaties or the Interest and Royalties Directive (see below).

# Withholding tax exemption under the Interest and Royalties Directive

Under the Interest and Royalties Directive, interest and royalties are exempt from Italian WHT if the following conditions are satisfied.

I. The beneficial owner of the interest or royalties is a company of another EU Member State or a permanent establishment situated in another EU Member State of a company of an EU Member State.

- II. The payer and the beneficial owner are companies (or permanent establishments of companies) that fulfil the requirements established in Annexes A (legal form) and B (liability to tax) of Presidential Decree no. 600/73 (these requirements correspond to those of the Directive).
- III. The payer and the beneficial owner are associated in one of the following ways.
  - a. The first company directly holds at least 25 percent of the voting rights in the second company.
  - b. The second company directly holds at least 25 percent of the voting rights in the first company.
  - c. A third company, which fulfils the requirements established in Annexes A and B of Presidential Decree no. 600/73, directly holds at least 25 percent of the voting rights in both the first and the second company.

These equity interests must be held for an uninterrupted period of at least one year.

Under article 15 of the Savings Agreement of 26 October 2004 between the European Union and Switzerland (providing for measures equivalent to those laid down in the EC Savings Directive 2003/48/EC), effective since 1 July 2005, outbound interest payments to companies resident in Switzerland are exempt under essentially the same conditions as those laid down in the EC Interest and Royalties Directive (2003/49/EC), except for the holding period (a two-year holding period is required in this case) and the reference to the 25 per cent holding of equity (instead of voting rights).

# 5.1.9 Tax consolidation

Both domestic and worldwide consolidation are available.

# Domestic tax consolidation

An Italian company and one or more of its Italian subsidiaries may opt for domestic tax consolidation, provided that the following conditions are fulfilled.

- The parent must directly or indirectly:
  - hold the majority of the voting rights at the subsidiary's shareholders' meeting;
  - II. hold more than 50 percent of the subsidiary's stated capital;
  - III. be entitled to more than 50 percent of the profits of the subsidiary.
- The parent and the subsidiaries must have the same tax year.
- The parent and each participating subsidiary must opt for tax

consolidation.

- The decision to opt for domestic tax consolidation must be indicated in the tax return filed for the first tax year of consolidation.
- Each subsidiary must opt to be domiciled for tax purposes at the domicile of the parent company.

Domestic tax consolidation lasts for three tax years and has various implications, some of which are listed below.

- The parent calculates the consolidated base, after each of the companies has calculated its own tax base in accordance with the ordinary IRES rules.
- The parent makes the periodic and final tax payments and may carry forward any net tax losses.
- Tax losses incurred by the consolidated companies during consolidation may be offset against the income of other consolidated companies.
- Tax losses incurred before the creation of the tax group may be offset only against the income of the company that has incurred them.
- Transfers of business assets are taxable in the ordinary way.
- The option is binding for three years and automatically renewed for another three years thereafter unless the participants opt out.
- Claw-back rules apply if the consolidation regime terminates early or is not renewed after three years.
- If the regime is interrupted early, the consolidating company alone may carry forward the tax losses incurred by the consolidated companies during the consolidation period. However, different criteria can be agreed between the regime participants.

Under the provisions in force until 2014, non-resident companies could opt for Italian tax consolidation only (i) as consolidating entities, (ii) if they were resident in a treaty country, and (iii) had a permanent establishment in Italy whose assets included shares/quotas in the Italian consolidated entities. In 2015, conditions (ii) and (iii) were repealed, in compliance with the principles set out in the European Court of Justice's judgment of 12 June 2014 in Case C-40/13.

Companies resident in Italy can be consolidated for tax purposes if they are controlled by a foreign company resident in a white-list EU/ EEA Member State. Permanent establishments in Italy of companies resident in a white-list EU/EEA Member State can also be consolidated. This form of consolidation requires the non-resident controlling entity to appoint an Italian controlled company as the consolidating entity.

# Worldwide tax consolidation

An Italian company may opt for worldwide tax consolidation with its non-resident subsidiaries provided that the Italian company is:

- I. listed on a regulated market, or
- controlled by the government, by a governmental entity, or by Italianresident individuals who do not directly or indirectly control other resident or non-resident companies.

Eligible non-resident subsidiaries are those in which the resident parent directly or indirectly holds more than 50 percent of the stated capital, voting rights and rights to profits. All of the following conditions must also be fulfilled.

- All of the non-resident subsidiaries must join the tax group (all-in or all-out).
- The parent company and the subsidiaries must have the same tax year.
- The financial statements of the consolidated entities must be audited.
- The non-resident subsidiaries must give written consent to the auditing of their financial statements and a written undertaking to cooperate with the parent company in determining the consolidated taxable income.

Worldwide tax consolidation is subject to approval by the Italian tax authorities, issued in the form of a ruling. This form of tax consolidation is valid for at least five years and automatically renewed for another three years thereafter unless the participants opt out.

Under the worldwide consolidation regime, the income of each nonresident subsidiary, determined in accordance with IRES rules (except for certain adjustments), is allocated to the parent company in proportion to its share in the profits of the subsidiary. Losses incurred before a company elects to join the tax group cannot be offset against income generated while the tax group is in place.

# 5.1.10 Consortium relief

The taxable income or tax loss of a qualifying Italian company can, by election, be allocated to its Italian corporate shareholders in proportion to their dividend rights. Companies with only corporate shareholders holding an interest of between 10 percent and 50 percent in the profits and in the voting rights of the company are qualifying companies. The option must be exercised jointly by the resident company and by all its shareholders.

The option is binding for three years and automatically renewed for another three years thereafter unless the participants opt out.

Non-resident corporate shareholders may opt for this regime on condition that no WHT is levied on the profits distributed by the Italian subsidiary. In practice, this requirement is satisfied only when the Parent-Subsidiary Directive applies.

Companies opting for tax consolidation do not qualify for this relief.

Tax losses carried forward by the shareholders and generated before election cannot be used to offset profits allocated under the consortium relief.

# 5.1.11 Anti-avoidance measures

# General anti-avoidance rules

# Recent changes

In a move to provide greater certainty in tax matters and improve the relationship between taxpayers and the Italian Revenue Agency, new measures were introduced in 2015. The 'wide-scope' anti-avoidance rule contained in article 37-*bis* of Decree no. 600/73 was repealed<sup>6</sup> and replaced by a new definition of 'abuse of law', effective from October 2015. The concepts of 'abuse of law' and 'tax avoidance' were merged and a definition of 'abuse of law' was given in the Taxpayers' Charter. Previously, the concept of 'tax avoidance' was defined by article 37-*bis* (see below), while 'abuse of law' was defined only by case law, without any legal definition.

This new definition is a broad one and no longer lists the transactions that are subject to the anti-avoidance rule. It applies to all income taxes and indirect taxes, except customs duties. Abuse of law arises when all the following factors are in play.

- I. The transaction (or series of interconnected transactions) has no economic substance (i.e. though valid on paper, it is an inappropriate way of achieving the stated business goal).
- II. An undue tax advantage is obtained, even without breaking any tax rule.
- III. The tax advantage is the essential effect of the transaction.

The concept of abuse of law applies only when a transaction cannot be assessed under a specific anti-avoidance measure. If an abusive transaction is discovered by the Italian Revenue Agency, it will be disallowed for tax purposes and the tax benefits will be denied. Transactions cannot be defined as abusive if they are justified by sound business reasons; these reasons include shake-ups or management decisions to improve the structure or operations of a business or professional activity. It is up to the Italian Revenue Agency to prove that

<sup>6</sup> By Legislative Decree no. 128 of 5 August 2015, which came into force on 2 September 2015.

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a transaction is abusive, while the taxpayer has to demonstrate that there is a sound business purpose. No criminal penalties can be applied – just administrative sanctions.

# The previous 'general' anti-avoidance rule

The former 'wide-scope' anti-avoidance rule (article 37-*bis* of Decree no. 600/73), repealed in 2015 and still applicable to notices of assessments served by 1 October 2015, stated that transactions (or a series of interconnected transactions) executed for no valid business reason, and aimed at circumventing tax obligations or obtaining illegitimate tax reductions or reimbursements, could be disallowed for tax purposes. However, this rule was not truly 'general' because it applied only to income taxes and a list of transactions, including the following:

- transformations, mergers and demergers, voluntary liquidations, and distributions of reserves not formed by retained earnings;
- contributions, transfers and leases of business units;
- transfers of receivables;
- · transfers of tax credits;
- the transactions indicated in Directive 90/434/EEC (mergers, demergers, spin-offs, and exchanges of shares with EU companies);
- changes of tax residence;
- share and foreign currency transactions, including evaluations;
- transfers of goods/services within a tax group (tax consolidation);
- interest/royalties paid between EU companies directly or indirectly controlled by a non-EU resident shareholder;
- penalties paid to related parties not resident in a white-list jurisdiction.

The tax authorities had to demonstrate that:

- the taxpayer had obtained a tax saving;
- the tax saving was undue;
- the purpose of the arrangement was to circumvent tax law (e.g. the transaction was not the typical or ordinary way of achieving a particular business goal).

The taxpayer had the burden of proving that there was a sound business purpose for the transaction, and not just a tax saving.

When an assessment was started under article 37-*bis*, the tax authorities would disallow the tax savings and compute and assess the taxes on the basis of the circumvented rule. They had to identify the circumvented rule and the 'typical arrangement' that the taxpayer should have made in order to obtain the desired result. They also had to show that the typical arrangement would have been feasible in the specific circumstances.

The application of penalties, especially criminal ones, was not straightforward and often questioned in domestic case law.

# Specific anti-avoidance tax measures

A number of Italian tax rules are designed to prevent tax avoidance by Italian companies in transactions with entities located in tax havens. These rules regard the following:

- a. deduction of black-list costs and expenses (repealed as of 2016);
- b. tax residence of foreign companies and entities (including trusts);
- c. CFCs;
- d. full taxation of capital gains arising from the transfer of shares in black-list companies;
- e. full taxation of inbound black-list dividends;
- f. anti-hybrid measures;
- g. transfer pricing.

# Deduction of black-list costs and expenses

Limitations to the deductibility of black-list costs and expenses applied up until the end of the tax year in progress on 31 December 2015.

So-called black-list costs and expenses arise from transactions with related or unrelated companies or undertakings resident or located in a black-list jurisdiction or territory.

Until the 2014 tax year, such costs and expenses were only deductible if the resident taxpayer, in an advance ruling application, or upon request by the authorities, could demonstrate one of the following:

- That the other party to the transaction engaged in an actual industrial or commercial activity in the jurisdiction where it was based (economic substance).
- That there were sound business reasons for the transaction and that the transaction had actually taken place.

Moreover, the resident taxpayer had to give separate evidence of such costs in its income tax return.

This rule did not apply if the other black list party was a controlled company and the CFC rule applied to it (see below).

In the 2015 tax year, black-list costs and expenses were fully deductible if at arm's length. For any portion exceeding the arm's length amount it was necessary to demonstrate the business rationale behind the transaction (while the first safe-harbour rule, requiring evidence of the business vitality of the foreign counterparty, was repealed). The resident taxpayer had to give separate evidence of black-list costs in its income tax return, regardless of whether these expenses were at arm's length or not.

An advance tax ruling could be requested in order to demonstrate that the safe-harbour rule had been met and secure the full deduction. The Black List for Cost Deduction only contained countries not allowing an adequate exchange of information.

# Black List for Cost Deduction

### Article 1

Andorra, Barbados, Barbuda, Brunei, Commonwealth of the Bahamas, Cook Islands, Djibouti (formerly Afars and Issas), French Polynesia, Grenada, Guatemala, Kiribati (formerly the Gilbert Islands), Lebanon, Liberia, Liechtenstein, Macau, Maldives, Marshall Islands, Nauru, New Caledonia, Niue, Oman, Saint Helena, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Samoa, Sark (Channel Islands), Seychelles, Solomon Islands, Tonga, Tuvalu (formerly the Ellice Islands), US Virgin Islands, and Vanuatu.

### Article 2

- Bahrain, with the exception of companies operating in the oil exploration, extraction and refining industry.
- Monaco, with the exception of companies that make at least 25 percent of their turnover outside the Principality.

### Article 3

- Angola, with respect to (i) oil companies that benefit from the exemption from oil income tax, (ii) companies which benefit from tax exemptions or reductions in industries essential to the Angolan economy, and (iii) investments indicated in the Foreign Investment Code.
- Antigua, with respect to (i) international business companies that operate abroad, such as those falling under the International Business Corporation Act no. 28 of 1982 (as subsequently amended), and (ii) companies that manufacture authorised products such as those falling under Law no. 18 of 1975 (as subsequently amended).
- Dominica, with respect to international companies operating abroad.
- Ecuador, with respect to companies operating in free-trade zones that benefit from the income tax exemption.
- Jamaica, with respect to (i) companies manufacturing for export and reaping the tax benefits of the Export Industry Encouragement Act, and (ii) companies located in territories indicated in the Jamaica Export Free Zone Act.
- Kenya, with respect to companies established in the export processing zones.
- Panama, with respect to (i) companies deriving income from foreign sources, as defined under Panama legislation, (ii) companies located in the Colón Free Zone, and (iii) companies operating in the export-processing zone.
- Puerto Rico, with respect to (i) companies engaged in banking activities, and (ii) companies falling under the Puerto Rico Tax Incentives Act of 1988 or the Puerto Rico Tourist Development Act of 1993.
- Switzerland, with respect to companies not subject to cantonal and municipal taxes, such as holding, auxiliary and 'domiciliary' companies.
- Uruguay, with respect to (i) companies engaged in banking activities, and (ii) holding companies that only operate offshore.

In the case of the jurisdictions listed in the third article, the black-list rule also applies to other businesses (regardless of their form) that benefit from a tax arrangement substantially similar to those indicated, because of a special measure issued by, or agreement concluded with, the local tax authorities.

As of the tax year following that in progress on 31 December 2015, the black-list cost regime was repealed to allow all costs according to the general rules only, including the arm's length principle (see previous page).

As clarified by the Italian tax authorities in Ministerial Circular no. 39/2016, the obligation for a resident taxpayer to give separate evidence of black-list costs in its income tax return has also been repealed. Moreover, the Black List for Cost Deduction, although not explicitly repealed, should no longer be considered.

# **Tax residence**

# Foreign companies and entities

Foreign companies and entities that own a controlling interest in an Italian company are deemed to be tax resident in Italy in either of the following cases.

- a. The foreign company/entity is, in turn, directly or indirectly controlled by an Italian individual or entity.
- b. The majority of the members of the board of directors of the foreign company/entity are Italian residents.

Unless there is evidence to the contrary, a non-resident company is also presumed to be resident in Italy if (i) most of its assets are units of Italian closed-end REIFs, and (ii) it is directly or indirectly controlled by a resident company or individual.

### Foreign trusts

Foreign trusts are deemed to be Italian residents (unless there is evidence to the contrary), if both of the following apply.

- They are not established in a white-list country.
- At least one of the settlors and at least one of the beneficiaries are resident in Italy.

Italian tax residence is also triggered if an Italian resident (i.e. settlor) transfers real estate or property rights to a trust that has been set up in a country not on the White List.

### Moving tax residence to Italy: tax basis of assets and liabilities

If a non-resident entrepreneur or enterprise changes residence and moves to Italy from a white-list country, the Italian tax basis of the business assets and liabilities will be their current market value. If the move is from a country that is not on the White List, the current market value must be determined in agreement with the tax authorities, via the international ruling procedure<sup>7</sup>. If no agreement is reached or requested,

<sup>7</sup> See the section below, headed 'International Rulings'.

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the tax basis is the purchase cost, book value or market value: for assets it is the lowest of these; for liabilities it is the highest.

# Moving tax residence outside Italy

If an Italian company moves abroad, this is (in principle) treated as a deemed disposal of the company's assets. The assets are deemed to be realised at their market value and any corresponding capital gain is subject to income tax in Italy, unless the assets are allocated to a permanent establishment in Italy.

Resident companies which transfer their registered office to an EU/EEA white-list Member State can opt to defer the taxation of the deemed gains, if the destination country is 'qualifying' (i.e. has concluded a mutual assistance agreement for the collection of taxes with Italy that is in line with the assistance guaranteed under the Council Directive 2010/24/EU of 16 March 2010 concerning mutual assistance for the recovery of claims relating to taxes, duties and other measures).

An Italian company that transfers its tax residence to a qualifying country may elect to do one of the following, instead of immediately paying the full tax on the deemed gain.

- Defer the taxation of the deemed gain on certain assets.
- Pay the tax on the deemed gain in six annual instalments.

Under the deferral regime, the company must comply with specific reporting obligations.

Any of the following events terminate the deferral regime and the instalment regime.

- The company transfers its residence from a qualifying country to another jurisdiction that is not a qualifying country.
- The company liquidates and winds up.
- The company undergoes a merger or a demerger that entails the transfer of the company's business to a jurisdiction that is not a qualifying country.

The tax deferral regime is also possible in the transfer of an Italian permanent establishment and the transfer of residence from Italy to an EU/EEA Member State as a result of a cross-border merger, demerger or contribution of a going concern.

# Controlled foreign company ("CFC") rules

Until the end of the tax year in progress on 31 December 2015, a CFC was a company resident or established in a black-list state or territory and in which an Italian resident directly or indirectly – even through a trust company or other third party – held the majority of votes or exercised a dominant influence.

A black-list state or territory meant one of the jurisdictions listed in the Ministerial Decree of 21 November 2001, i.e. jurisdictions offering a level of taxation 'significantly lower' than in Italy or an inadequate exchange of information with the Italian Revenue Agency.

A CFC can also be resident or established in a country (including EU Member States) that is not on the CFC Black List, provided that (i) the CFC's ETR is less than half of the Italian ETR that would apply if the CFC were tax resident in Italy, and (ii) the CFC's income is mainly passive or originates from related-party transactions.

Under the CFC regime, an Italian resident is subject to tax on profits realised by the CFC.

As of the tax year following that in progress on 31 December 2015, these anti-avoidance measures were further amended. The new rule identifies 'black CFCs' as those companies resident or established in states or territories, other than EU Member States or States in the EEA (i.e. Norway or Iceland or Liechtenstein), whose tax regimes (ordinary or special) grant a nominal level of taxation of less than half the level of corporate taxation in Italy.

# Safe-harbour rules

For protection from the CFC rules, in the case of a 'black CFC' (according to the above definition), an Italian taxpayer must be able to prove, in its application for an advance ruling or upon request by the tax authorities, one of the following.

- That, as its core business, the black CFC actually trades on the market of the state or territory in which it is located (business test).
- b. That at least 75 percent of the income of the black CFC is subject to tax in a state or territory whose nominal level of taxation is equal to or higher than 50% of the level of corporate taxation in Italy, the EU or EEA (i.e. Norway or Iceland or Liechtenstein) (subject-to-tax test).

With specific regard to CFCs resident or established in countries that are not 'black' (i.e. countries that don't have a nominal level of taxation of less than half the level of taxation in Italy), an Italian taxpayer can avoid being taxed on the CFC's income only if it can prove that the CFC **is not an artificial structure.** 

# Effects of the CFC rules

The income subject to tax in Italy is computed in accordance with the Italian rules and taxation is separate (e.g. any available tax loss carry-forwards cannot shelter the CFC income).

Dividends originally paid by a CFC located in a state or territory that is 'black' for CFC purposes (i.e. since 2016, one with a nominal level of taxation of less than half the level of taxation in Italy) and that only passes the business test are taxed in full to the ultimate Italian recipient (i.e. no Participation Exemption); whereas those paid by an entity passing the subject-to-tax test qualify for the 95 percent exemption<sup>8</sup>.

# Recent developments

The 2015 Growth and Internationalisation Decree introduced the following amendments to the CFC rules, with effect from 1 January 2015.

- Advance rulings, formerly required to exclude the application of CFC rules, are no longer mandatory and the taxpayer may provide evidence of safe-harbour conditions during a tax audit. However, if an advance ruling is not requested or the outcome of the ruling is unfavourable, the investment must be reported separately in the income tax return. There are special penalties for failure to comply with this reporting requirement.
- Before issuing a notice of assessment focussing on CFC income, the tax authorities must allow the taxpayer to provide evidence of safe-harbour conditions. The notice of assessment can be issued only 90 days after a formal request for further information; otherwise it is invalid. Any tax assessment notice must include specific comments on the information provided by the taxpayer.
- The CFC regime no longer applies to companies which a resident taxpayer does not control (de facto or through voting rights or) but in which the resident taxpayer owns at least a 50 percent stake through a share in profits.

<sup>8</sup> See the section headed 'Tax treatment of dividends and capital gains and losses'.

 For CFCs in jurisdictions (including EU Member States) that are not 'Black', the Italian Revenue Agency issued a statement of practice identifying the simplified criteria to be used in assessing whether the ETR of a CFC is less than half the ETR that would apply if it were resident in Italy.

# CFC Black List published in the Decree of 21 November 2001 (modified by the Decree of 30 March 2015 and repealed as of 2016)

# Article 1

Alderney (Channel Islands), Andorra, Anguilla, Aruba, Commonwealth of the Bahamas, Barbados, Barbuda, Belize, Bermuda, British Virgin Islands, Brunei, Cayman Islands, Cook Islands, Djibouti (formerly Afars and Issas), French Polynesia, Gibraltar, Grenada, Guatemala, Guernsey (Channel Islands), Herm (Channel Islands), Hong Kong, Isle of Man, Jersey (Channel Islands), Kiribati (formerly the Gilbert Islands), Lebanon, Liberia, Liechtenstein, Macau, Maldives, Marshall Islands, Montserrat, Nauru, Netherlands Antilles, New Caledonia, Niue, Oman, Saint Helena, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Samoa, Sark (Channel Islands), Seychelles, Solomon, Tonga, Turks and Caicos Islands, Tuvalu (formerly the Ellice Islands), US Virgin Islands, and Vanuatu.

# Article 2

- Bahrain, with the exception of oil exploration, extraction and refining companies.
- United Arab Emirates, with the exclusion of the companies operating in the oil and petrochemical industries and subject to tax.
- Monaco, with the exception of companies that make at least 25 percent of their turnover outside the Principality.

# Full taxation of capital gains arising from the transfer of shares in companies located in low-tax jurisdictions<sup>9</sup>

In general, capital gains realised on the disposal of shares in foreign companies are treated just like domestic gains and are 95 percent exempt (this is called the Participation Exemption). This exemption is conditional upon the foreign company being resident in a "white-list" country for three years.

On the contrary, capital gains realised on the disposal of shares in companies located in low-tax jurisdictions as per the definition provided for CFC rules, are taxed in full.

# Full taxation of inbound dividends<sup>10</sup>

Dividends paid by companies located in a country that can be defined as 'black' under the CFC rule (see above) are generally taxable in the hands

<sup>9</sup> See the section headed 'Tax treatment of dividends and capital gains and losses'.10 See the section headed 'Tax treatment of dividends and capital gains and losses'

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of the resident (corporate) shareholder at the full CIT rate on 100 per cent of their amount, unless a safe-harbour rule applies (subject-to-tax test).

### Anti-hybrid rule.

The 95 percent dividend exemption is granted on condition that the payment is not deductible by the non-resident payer and that the payer declares this.

### Transfer pricing rule

This measure will be dealt with in section 6.

# 5.1.12 Foreign tax credits

Taxes paid on foreign business income are creditable against the IRES due, up to the portion of IRES that corresponds to the ratio of foreign income to total income (net of any tax loss carryforwards). This limit applies to each country.

The credit should be claimed in the tax return for the year in which the foreign income must be declared, on condition that the foreign tax payment is definitive before the deadline for submission of the tax return. Should the foreign income be partially exempt (as in the case of foreign dividends) the creditable foreign tax is reduced proportionally.

More favourable conditions may be available under double tax treaties. Some treaties in force with Italy still include 'matching credit' or 'tax sparing' clauses, which allow Italian investors to credit notional foreign taxes, irrespective of the actual or lower payments made in the country of source (due, for instance, to local tax incentives).

When business income is earned through foreign permanent establishments or a non-resident company included in a worldwide tax consolidation arrangement, any surplus credit can be carried back for up to eight years and offset against IRES on the same type of income from the same country. If there is not enough IRES for this, the surplus credit can be carried forward for up to 8 years.

From 1 January 2015, the rules previously applying only to taxes paid by a foreign permanent establishment (such as the carry-back option for surplus foreign tax credits) were extended to all types of foreign income earned by an Italian company.

Moreover, foreign tax credits are now granted for all types of foreign income tax payments, whether or not they fall within the definition of foreign income tax payments found in the relevant tax treaty with Italy. Uncertain cases should be cleared in advance with the Italian Revenue Agency.

# 5.1.13 Tax rulings

# Ordinary tax rulings

From 1 January 2016, there will be a new classification of tax ruling procedures, with five types of ruling.

- a. 'Interpello ordinario', for an interpretation of unclear tax rules in a pending case.
- b. 'Interpello qualificatorio', for a legal definition of pending transactions that do not clearly fit the definitions provided by tax law.
- c. 'Interpello probatorio', for confirmation that a taxpayer qualifies for certain tax benefits or tax regimes (e.g. the advance tax ruling that can be requested in order to prove that the CFC safe-harbour conditions apply<sup>11</sup>).
- d. 'Interpello antiabuso', to understand whether the new abuse of law rule applies to one or more transactions<sup>12</sup>.
- e. 'Interpello disapplicativo', which should be filed beforehand, to allow the disapplication of specific anti-avoidance measures (e.g. measures to limit loss carryforwards of companies involved in a merger or demerger and prevent dividend washing).

These five categories of ruling are governed by the same rules, which cover aspects such as the timing of applications, eligibility to apply, investigation procedures and causes of inadmissibility. For instance, ruling applications must be submitted before the deadline for submission of the tax return or fulfilment of the other tax obligations queried in the application. However – and this marks a considerable change from the previous rules – the tax authorities may respond after this deadline. Only in the case of an '*interpello ordinario*' and '*interpello qualificatorio*' must the Italian tax administration reply within 90 days. For other categories of ruling, the Italian tax administration must reply within 120 days. In all cases, if the tax administration requires additional documentation, the response time can be deferred by 60 days, only once.

If the tax administration does not respond within the above-mentioned time frames, the solution proposed by the taxpayer is deemed to have been accepted by the tax authorities.

On 4 January 2016, the Director of the Revenue Agency issued a regulation containing implementing measures; moreover, the tax

<sup>11</sup> See the above section headed 'Controlled foreign company rules'.

<sup>12</sup> See the above section headed 'General anti-avoidance rules'.

authorities issued Ministerial Circular no. 9 of 1 April 2016, outlining the main features of the new ruling procedure.

# New form of ruling for substantial investments

Since 20 May 2016, a new form of tax ruling has been available for companies that intend to invest a minimum of EUR 30 million in Italy, generating new employment. The idea is to provide greater certainty about the income generated by such investment plans and the wider tax implications. With its application for a ruling, the investor, whether resident or non-resident, must present a business plan indicating the size of the investment, its timing and mode of implementation, and the number of workers who are likely to be hired. The investor may ask for a tax ruling on various issues, including, for example, whether abuseof-law or other anti-avoidance measures are likely to be triggered, the tax implications of a group reorganisation, and whether certain assets constitute a going concern. The tax authorities should provide the investor with a written answer within 120 days. If the tax administration does not respond within the above-mentioned time frames, the solution proposed by the taxpayer is deemed to have been accepted by the tax authorities. The answer is binding as long as the facts and circumstances do not change.

# International rulings

International rulings are for companies that have international business operations. The following types of companies can apply for an international ruling;

- resident companies that satisfy transfer pricing requirements;
- resident companies owned by or owning non-resident companies;
- resident companies that have paid interest, dividends or royalties to non-residents or have been paid these by non-residents;
- non-resident companies that operate in Italy through a permanent establishment.

Through an international ruling it is possible to:

- predefine the transfer pricing methods to be used in calculating the arm's length value of transactions;
- clarify how to apply the rules, including treaty rules, on the:
  - payment to (or receipt from) non-residents of dividends, interest, royalties or other income;
  - allocation of gains or losses to permanent establishments.
- clarify whether a multinational enterprise has a permanent establishment in Italy, under Italian tax law and tax treaties;

 respond to queries about the tax basis of assets and liabilities in a transfer of residence (to Italy or from Italy to a different EU Member State)<sup>13</sup> and about the arm's length value of black-list costs.

The application must be filed with the Revenue Agency in Milan or Rome, depending on where the applicant is domiciled for tax purposes, and must be accompanied by full documentary proof that the applicant is eligible for an international ruling.

However, before filing an application, taxpayers may ask for a meeting with the tax authorities (also on an anonymous basis) for further information on the procedure.

The process should be completed within 180 days of filing the application, but in practice – especially for rulings on transfer pricing matters – it takes much longer, as several meetings between the taxpayer and Revenue Agency are generally necessary, as well as double-checks.

So that it can collect the information it requires, the Revenue Agency has access to the sites where the company or permanent establishment operates. The Revenue Agency may also seek the cooperation of foreign tax administrations, in which case the 180-day time limit may be suspended until the information requested from the foreign tax administration has been obtained.

To complete the process, the taxpayer and the Revenue Agency must sign an agreement. This is binding for five years and prevents the Revenue Agency from carrying out any tax assessment of the matters that it regulates. A report will be issued if the parties fail to reach an agreement.

Once the agreement is signed, the taxpayer must submit documents and information, either periodically or upon request by the tax authorities, to let the Revenue Agency control compliance with the agreement.

Partial or total violation of the agreement results in its cancellation. The agreement will also be rescinded if there are any material changes in the facts or the law. Therefore, the company must keep the Revenue Agency informed of any new circumstances and give it free access to its records.

Before the agreement expires, the taxpayer can apply to renew it.

<sup>13</sup> See the above section entitled 'Moving to Italy: tax basis of assets and liabilities'.

Renewal (or changes) may involve an inquiry or further discussions between the Revenue Agency and the taxpayer.

For a transfer pricing ruling, the applicant must illustrate the criteria and methods that it intends to use in calculating the arm's length values of the transactions, and explain why it thinks these are the right ones. It must also produce the relevant documentation. If the ruling regards other matters, the applicant must indicate which of the legally available solutions it advocates, and why it considers this solution to be in accordance with the law.

The international ruling procedure can also be used to clarify whether a multinational enterprise has a permanent establishment in Italy, under Italian tax law and tax treaties. The ruling is binding for 5 years (unless there are changes in the circumstances or law).

The international ruling procedure has recently been extended so that it can be used for queries about the tax basis of assets and liabilities in a transfer of residence (to Italy or from Italy to a different EU Member State) and about the arm's length amount of black-list costs.

# Advance Pricing Agreements

APAs, which are a form of international ruling specifically applicable to transfer pricing matters (usually bilateral or multilateral), are also available and are binding for five years.

# 5.2 Partnerships

# 5.2.1 Determination of taxable income

Italian partnerships are tax-transparent and are not included in the list of taxpayers subject to CIT. Income is allocated to partners whether or not it is actually paid. However, just like the income of companies subject to CIT, the income of both a general partnership('società in nome collettivo' or 'Snc') and a limited partnership ('società in accomandita semplice' or 'SAS') is always treated as business income, even if it includes other categories of income, such as capital income or miscellaneous income. Such income is allocated and taxed to the partners as business income, in proportion to their contributions, whether or not they are entrepreneurs.

The income of an Italian partnership that is allocated to non-resident partners is always taxed in Italy as business income, even if the nonresident partner has no permanent establishment in Italy.

As of 1 January 2017, general partnerships can opt for a new tax regime called IRI, provided that they use ordinary accounting methods (meaning that they do not use simplified accounting methods, which may be

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used by businesses meeting certain specific requirements stipulated by law). This IRI regime, derogating the transparency principle, allows the partnership to be taxed at a rate of 24 percent on the income that remains within it. General partnerships may opt for this IRI regime in their tax return for the 2017 tax year. The regime runs for five years and is not renewable.

# 5.2.2 Foreign partnerships

Under Italian tax laws, non-resident entities (whether partnerships or corporations) are never considered to be transparent entities. Therefore, for Italian tax purposes, a foreign partnership is always similar to a corporation. Should it earn income from Italy, it will be subject to IRES.

However, the Italian income attributed to the non-resident partnership is not heaped together and treated as business income but is calculated in accordance with the specific rules established for each single category of income (capital income, real estate income, etc.). Only if the nonresident partnership has a permanent establishment in Italy will the income generated by the permanent establishment be considered (and calculated) as business income.

According to the Italian Revenue Agency<sup>14</sup>, if a partnership cannot be considered as tax resident in a treaty country, because the partnership's income is allocated to its partners for taxation in their country of residence, then Italy should grant the benefits provided by the treaty entered into by the states in which the partners are resident. By contrast, where the foreign partnership is considered as a corporation under the domestic law where it is resident (in general, when it is not considered as transparent), it can qualify as a 'person resident' in a contracting state for treaty purposes and is entitled to treaty benefits.

# Entitlement of foreign transparent entities to treaty benefits

Official interpretations on foreign transparent entities generally concern their entitlement to treaty benefits. Usually, transparent entities are not deemed to be resident for treaty purposes and therefore are not entitled to treaty benefits. Investors in the transparent entity are entitled to treaty benefits if they fulfil the following conditions<sup>15</sup>.

- They qualify as ' resident persons' and are therefore 'liable to tax' in their country of residence.
- They are the beneficial owners of the partnership income.

With respect to the first condition, issues will arise if the investor itself is an entity, such as a collective investment vehicle (e.g. a pension fund or real estate trust), which is exempt from income taxes in its country

<sup>14</sup> See the interpretation given in Italian Revenue Agency Notice no. 306/1996. 15 See Italian Revenue Agency's Rulings no. 17/2006 and no. 167/2008.

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of residence. In this case, a certificate of residence issued by the tax authorities of the country of residence of the investor/fund is required.

Regarding dividends paid by Italian companies to an Irish CCF (common contractual fund), the Italian Revenue Agency has clarified that, since a CCF is a transparent entity not subject to tax on its income, it is not entitled to treaty benefits. Moreover, in order for the fund investors to be entitled to the benefits of the treaty in force between Italy and their country of residence, two conditions must be met.

- a. The articles of the fund must provide for the annual distribution of profits.
- b. Distributions must be subject to tax in the country of residence of the investors.

Regarding the tax treatment of proceeds (dividends and capital gains) from investments made by a pension fund, set up under the law of the Netherlands, in Italian companies held through a Luxembourg FCP, the Italian Revenue Agency has clarified<sup>16</sup> that:

- the FCP cannot be deemed to be a 'resident person' for treaty purposes as it is fiscally transparent and not subject to unlimited tax liability in Luxembourg;
- consequently, the treaty in force between Italy and Luxembourg is not applicable to proceeds distributed to the FCP.

In compliance with the OECD Commentary on Article 5, the treaty between Italy and the Netherlands – the country of residence of the investor (the pension fund) – is applicable, provided that the investor is entitled to the treaty benefits. This means that it must be 'resident' for treaty purposes in the Netherlands and be the beneficial owner of the income. As proof that these two conditions are satisfied, the Italian tax administration requires the following.

- a. The articles of the FCP must provide for annual distribution of profits.
- b. The proceeds from distribution must be subject to tax in the country of residence of the pension fund.
- c. The pension fund, even though exempt, must be subject to corporate income tax in the Netherlands, as stated in a certificate issued by the tax authority.

<sup>16</sup> In Ruling no. 167/2008.

# 5.3 Permanent establishments

# 5.3.1 Definition of permanent establishment

For IRES and IRAP purposes a permanent establishment is a fixed place of business through which the business of a non-resident enterprise is wholly or partly carried on in Italy. The ITC gives a list of examples that are presumed to constitute a '**fixed-place permanent establishment**', unless the taxpayer gives evidence to the contrary: (i) a place of management, (ii) a branch, (iii) an office, (iv) a factory, (v) a workshop, and (vi) a mine, an oil or gas well, a quarry or other place for the extraction of natural resources. However, a fixed place of business is not deemed to be a permanent establishment in Italy if it is used only to perform certain preparatory or auxiliary activities. Moreover, computers and auxiliary equipment for the collection of information and the transmission of data for the sale of goods or services do not by themselves constitute a permanent establishment.

A resident or non-resident person that habitually concludes contracts in Italy in the name of a non-resident enterprise, other than for the purchase of goods, is deemed to be an '**agency permanent establishment**' in Italy of the non-resident enterprise. However, the mere fact that a non-resident enterprise pursues its activity in Italy through a broker, general commission agent or any other agent of an independent status does not constitute a permanent establishment, provided those persons act in the ordinary course of their business. Moreover, the fact that a non-resident enterprise controls a resident enterprise, or is controlled by it, or that the two enterprises are both controlled by the same third entity, does not of itself make either of these enterprises a permanent establishment of the other.

The domestic definition of permanent establishment is substantially consistent with the definition given by the OECD Model Convention. There are, however, a few differences.

- Length of time necessary to fulfil the permanency requirement for a building site: this is three months in domestic law and 12 months in the OECD Model Convention.
- Supervisory activity in connection with a building site: this is included in the definition of a permanent establishment given by domestic law but not in the definition given in the OECD Model Convention.

- Preparatory and auxiliary activities combination of activities: domestic law lists a series of ways in which a fixed place of business can be used without giving rise to a permanent establishment, in line with the current OECD Model Convention. But it differs from ordinary Italian tax-treaty negotiation practice because the last of the listed ways – a combination of activities that, viewed as a whole, constitutes a preparatory or auxiliary activity – does not appear in the lists found in the treaties concluded by Italy. However, this does not seem to result in any material difference as the more advantageous domestic rule should prevail.
- Electronic commerce: domestic law states that "the availability of computers and other auxiliary systems that enable the collection and transmission of data and information for the sale of goods and services does not constitute, of itself, a permanent establishment" [KPMG unofficial translation], while this less stringent rule is not in the OECD Model Convention.
- Agency permanent establishment: under domestic law, "a resident or non-resident person who habitually concludes contracts in Italy in the name of a non-resident enterprise, other than for the purchase of goods, constitutes a permanent establishment in Italy of the non-resident enterprise" [KPMG unofficial translation]. Unlike the OECD rule, this does not require the agent to act on behalf of the non-resident enterprise; nor does it expressly require the agent to have an authority to conclude contracts in the name of the enterprise. Moreover, according to the OECD Model Convention, a dependent agent does not give rise to a permanent establishment if his activities are of an auxiliary or preparatory nature; whereas, according to Italian law, the exclusion only applies to the purchase of goods. In practice, however, in light of case law (in its observations on the Commentary, Italy states that its jurisprudence is not to be ignored in interpretation of the agent permanent establishment definition in the OECD Model Convention), the fact that the resident person acts 'on behalf', even if not in the name, of the non-resident is seen as a symptom of dependence; moreover, the exclusion for preparatory and auxiliary activities also applies to agents.
- Control: according to Italian law, the fact that a non-resident enterprise controls a resident enterprise, or is controlled by it, or that the two enterprises are both controlled by the same third entity, does not of itself make either of these enterprises a permanent establishment of the other. The Italian rule is broader than the one found in the OECD Model Convention as it includes companies under common control.
- Moreover, under Italian law a permanent establishment has specific features when it is involved in the gaming business (which it does not under the OECD Model).
- So far, BEPS proposals included in Action 7 have not been officially implemented in Italy, although they are largely used as a source of interpretation in OECD MC scenarios.

5.3.2 Determination of taxable income

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An Italian permanent establishment of a foreign company is subject

to both IRES and IRAP on income from business in Italy. The taxable income is calculated in accordance with the rules applicable to resident companies.

No branch remittance tax is currently imposed on net profit transferred to the head office, whether or not the head office is located within the EU.

The attribution of profit to the permanent establishment now follows the approach of the OECD Model Convention (*'these profits are the profits that the permanent establishment might be expected to make if it were a separate and independent enterprise'*) and of the 2008 and 2010 OECD reports on attribution of profits to permanent establishments. So-called *'internal dealings' between a permanent establishment and its own foreign headquarters must also be at arm's length.* 

A newly-introduced 'branch-exemption' regime allows a resident taxpayer, as of 2016, to opt for the exemption of all its foreign branches (all or nothing). If there are branches that are established in a country that is considered 'black' for CFC purposes or have (i) an ETR less than half of that in Italy and (ii) mainly passive income (see the above section on 'Controlled foreign company rules'), the branch exemption will not apply and the income of such branches will be imputed to the Italian headquarters like CFC income. By contrast, if such 'CFC branches' comply with the safe-harbour rules (again, see the above section on 'Controlled foreign company rules'), the branch exemption remains available.

Certain claw-back rules apply if such branches are loss-making before the election is made.

An implementing Decree should have been issued by March 2016, but still has not. Therefore, although the regime is theoretically in force, some important aspects are still not clear.

# 5.4 EU directives, regulations and agreements concerning direct taxation

The following EU rules on income taxation have been adopted by Italy.

 Council Regulation (EEC) No 2137/85 of 25 July 1985 on the European Economic Interest Grouping (EEIG) entered into force (in all EU

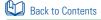


Member States) on 3 August 1985.

- Council Regulation (EC) No 2157/2001 on the Statute for a European company (SE) entered into force (in all EU Member States) on 8 October 2004.
- Council Directive 2001/86/EC supplementing the Statute for a European company with regard to the involvement of employees, was implemented by Legislative Decree no. 188 of 19 August 2005.
- Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards. This was implemented in Italian tax law through Legislative Decree no. 38/2005.
- Regulation (EC) No 1435/2003 on the Statute for a European Cooperative Society (SCE) entered into force (in all EU Member States) on 18 August 2006.
- Council Directive 2003/72/EC supplementing the Statute for a European Cooperative Society with regard to the involvement of employees was implemented by Legislative Decree no. 48 of 6 February 2007.
- Directive 2003/49/EC on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States was implemented by Legislative Decree no. 143 of 30 May 2005. Its provisions are contained in article 26-quater of Presidential Decree no. 600/73.
- Council Directive 2003/48/EC of 3 June 2003 on taxation of savings income in the form of interest payments was implemented by Legislative Decree no. 84 of 18 April 2005. This Directive was repealed by the EU Directive 2015/2060/EU and implemented in the Italian tax law.
- The EU-Swiss Savings Agreement of 26 October 2004 entered into force on 1 July 2005. Under article 15 of this Agreement, Switzerland must exempt interest and dividend payments made to companies resident in EU Member States under essentially the same conditions as those laid down in, respectively, the EC Interest and Royalties Directive and in the EC Parent-Subsidiary Directive.
- The Mutual Assistance Directive, as amended by Council Directive 2003/93/EC, was implemented by Legislative Decree no. 215 of 19 September 2005 (mutual assistance by the competent authorities of the Member States in the field of direct and indirect taxation).
- The Parent-Subsidiary Directive (Directive 90/435/EC of 23 July 1990), amended by Council Directives 2003/123/EC and 2011/96/EU of 30 November 2011 (recast) and, was implemented by Legislative Decree no. 49 of 6 February 2007. Its provisions are contained in article 27-*bis* of Presidential Decree no. 600/73. Directives 2014/86/EU and 2015/121/EU of 27 January 2015 introduced further

amendments to the Parent-Subsidiary Directive, which have been implemented in the Italian tax law.

- Directive 2009/133/EC of 19 October 2009, as amended in 2013, on the common system of taxation applicable to mergers, divisions, partial divisions, transfers of assets and exchanges of shares concerning companies of different Member States and to the transfer of the registered office of an SE or SCE between Member States. This Directive, which repealed Directive 90/434/EEC, was implemented by Legislative Decree no. 199 of 6 November 2007 and its provisions are contained in articles 178-181 ITC.
- On 30 May 2008, the Italian government passed Legislative Decree no. 108 to implement (in Italian civil law) the directive on cross-border mergers of limited liability companies.
- Directive 2013/34/EU, regarding certain elements of the corporate governance statement, was brought into Italian law through Legislative Decree no. 139 of 18 August 2015. New provisions, which amend the rules of civil law on financial statements of resident companies, will enter in force from 1 January 2016.
- Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation (repealing Council Directive 77/799/EEC). This directive was amended by Council Directive 2014/107/EU of 9 December 2014 (which extends the scope of the automatic exchange of information) and implemented in the Italian tax law.
- Convention 90/436/EEC on the elimination of double taxation in connection with the adjustment of profits of associated enterprises of 23 July 1990, ratified in Italy by Law no. 99 of 22 March 1993, introduced a Mutual Agreement Procedure.
- The Anti-tax avoidance (or ATAD 1) Directive (Directive 2016/164 of 12 July 2016) have been implemented in the Italian tax law.



# 6. Transfer pricing

# 6.1 General principles

Italian transfer pricing regulations are included in the corporate income tax rules, specifically in article 110(7) of Presidential Decree no. 917/1896 (the Corporate Income Tax Code). The regulations are based on the 1979 version of the OECD Transfer Pricing Guidelines, although in practice, the principles outlined in the 2010 version are generally recognised and applied by the Italian tax authorities in tax audits and rulings. The 2016 Budget Law introduced Country-by-Country reporting obligations to implement the measures included in the OECD's BEPS Action 13.

© 2017 KPMG S.p.A., KPMG Advisory S.p.A., KPMG Fides Servizi di Amministrazione S.p.A., KPMG Audit S.p.A., Italian limited liability share capital companies, and Studio Associato - Consulenza legale e tributaria, an Italian professional partnership, are member firms of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. The transfer pricing regulations are based on the "normal value principle" (basically the arm's length principle), whereby the conditions applied in an intra-group transaction should be comparable with those that would be applied between unrelated entities in comparable transactions. The tax authorities may apply this rule automatically if taxable income is thereby increased; conversely, a reduction of taxable income is only possible pursuant to the principles established by double tax treaties.

The test for the existence of arm's length conditions is based on the methods identified by the OECD Transfer Pricing Guidelines. Italian transfer pricing regulations consider the Comparable Uncontrolled Price (CUP) Method as the preferred method to be applied whenever possible. However, the principle that the most appropriate method to the circumstances of the case must be selected – established by the 2010 version of the OECD Transfer Pricing Guidelines – is commonly accepted and applied by the Italian tax authorities.

Transfer pricing regulations in Italy only apply to cross-border transactions between related entities (i.e. entities that directly or indirectly control the Italian company in question, are controlled by it or are under its joint control). The application of transfer pricing rules to domestic transactions, as seen in some instances of Italian case law, was recently excluded by article 5(2) of Legislative Decree no. 147/2015.

Transfer pricing rules apply for both corporate income tax (IRES) and local tax (IRAP) purposes.

# 6.2 Documentation issues

In drawing up transfer pricing documentation, reference is generally made to (i) the principles established in the OECD Guidelines, supplemented by the indications provided by the EU Transfer Pricing Code of Conduct issued by the EU Joint Transfer Pricing Forum, and (ii) Italian tax regulations.

Italian tax regulations establish a "penalty protection regime" for taxpayers that prepare transfer pricing documentation (article 26 of Law Decree no. 78/2010, converted into Law no. 122/2010 and supplemented by the guidelines issued on 29 September 2010 by the Italian tax authorities and the subsequent circular released on 15 December 2010). Recognition of penalty protection is subject to certain requirements: (i) that the taxpayer prepares in advance and discloses the existence of transfer pricing documentation to the tax authorities; (ii) that the taxpayer submits the documentation upon the request of the tax authorities in a timely manner; (iii) that the documents strictly comply with the template included in the tax authorities' guidelines; (iv) that the transfer pricing documentation be declared appropriate by the Italian tax authorities in the tax audit report. The transfer pricing documentation template provides for a Masterfile/Country File approach.

If the taxpayer is in possession of proper transfer pricing documentation, the burden of proof lies with the tax authorities, which, in tax audits resulting in adjustments to transfer prices, must give evidence of the criteria on which the transfer pricing adjustments are based. Conversely, a lack of documentation makes it easier for the tax authorities to justify a tax assessment and a transfer pricing adjustment and, therefore, shifts the burden of proof to the taxpayer, who must demonstrate that the tax authorities' approach is incorrect.

For certain transactions, such as intra-group services, general Italian corporate income tax rules require proof that the services are actually pertinent to the business, i.e. that the company receiving the services obtains - or can reasonably expect to obtain - an advantage from them, in consideration of its ordinary business activity. This circumstance must be demonstrated by appropriate (additional) documentation, which must be shown to the Italian tax inspectors in a tax audit. The Italian tax authorities have recently been taking a very aggressive approach to Italian companies that are members of multinational groups and deduct intra-group charges for services, usually disallowing the deduction if the charges are not appropriately documented.

# 6.2.1 Country-by-Country reporting

The 2016 Budget Law (article 1, paragraphs 145 and 146) introduced Country-by-Country reporting obligations, pursuant to the indications of the OECD's BEPS Action 13, for Italian resident parent companies of groups with a consolidated turnover in excess of EUR 750 million. The obligation also extends to Italian resident subsidiaries when the parent company is subject to the consolidated financial statements obligation but there is no County-by-Country reporting obligation or exchange of information concerning Country-by-Country reporting in its country of residence.

The country-by-country report must be submitted within 15 months of the last day of the tax year of the MNE Group to which it relates. The first country-by-country report must be sent for the tax year of the MNE Group commencing on or after 1 January 2016 within 18 months of the last day of that tax year.

Failure to comply with the Country-by-Country reporting obligation incurs an administrative penalty ranging from EUR 10,000 to EUR 50,000.

The terms and conditions of the Country-by-Country reporting measures will be established by means of a Ministerial Decree.

# 6.3 Penalties

In the event of a tax assessment, no penalties should apply if the taxpayer qualifies for the above penalty protection regime. Alternatively, standard corporate income tax penalties, modified by Legislative Decree no. 158/2015 and ranging from 90 to 180 percent of the additional tax, can be applied where higher taxable profits have emerged as a result of a transfer pricing adjustment. The taxpayer may, however, be able to reduce the penalties in the event of early settlement.

In certain circumstances, criminal penalties may also apply.

# 6.4 International Standard Ruling

The International Standard Ruling procedure covers both transfer pricing and other international taxation matters. With specific reference to transfer pricing, through the implementation of the procedure, unilateral, bilateral and multilateral Advance Pricing Agreements (APAs) have been introduced In Italy, which serve to define the methods to be used in calculating the arm's length value of transactions subject to transfer pricing regulations in advance. The ruling may also be used to determine the attribution of profits between a permanent establishment and its head-office and verify the existence of a permanent establishment in Italy of a foreign enterprise.

The International Standard Ruling scheme is reserved to "enterprises with international activity", namely:

- resident companies that meet the conditions imposed by current transfer pricing rules;
- resident companies owned by or owning non-resident companies;
- resident companies that have paid interest, dividends or royalties to non-residents or have been paid these by non-residents;
- non-resident companies that operate in Italy through a permanent establishment.

The APA procedure starts with an application, to be filed with the Revenue Office in Milan or in Rome, depending on the tax domicile of the applicant. The application must include all documents demonstrating that the applicant is eligible for the procedure. The Revenue Office may seek the international cooperation of foreign tax authorities. In this case, the deadline for completion of the procedure may be postponed until the information requested from the foreign tax authorities is obtained.

The process ends with the taxpayer and the director of the relevant Revenue Office signing an agreement that is binding on taxpayers and the Italian tax authorities for a five-year period, unless significant changes are made to the business of the applicant in that period.

Recently introduced regulations provide the taxpayer with the possibility of rolling back the effects of the agreement to the date the taxpayer requested it rather than the date it is signed, which may be two or three years later; the taxpayer may submit an amended income tax return in line with the transfer pricing mechanism in force in the years between the filing of the APA request and its signing, with just the interest due being applied.

Over the five tax years for which the agreement is valid, the tax authorities may only carry out tax assessments in relation to matters other than those covered by the agreement.

Should an agreement not be reached, a written report is drawn up.

Partial or total violation of the agreement leads to its cancellation. Furthermore, should there be any material changes in the facts or law, the agreement will be terminated. Therefore, the taxpayer is asked to periodically inform the Revenue Office of any changes and give it free access to the company.

Taxpayers can submit an application to renew the APA up to 90 days before its expiration. Amendments to the agreement and its renewal can both imply an inquiry or further debate between the Revenue Office and the taxpayer.



# 7. Taxation of individual income

# 7.1 General rules

# 7.1.1 Introduction

An individual's liability to Italian income tax is based on their residence status for taxation purposes and on the source of income.

The Italian tax year is equivalent to the calendar year (from 1 January to 31 December).

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# 7.1.2 Italian tax residents

Individuals who are tax resident in Italy are subject to income tax on their worldwide income, unless they are exempt under the provisions of a treaty.

An individual is considered to be an Italian resident for tax purposes, subject to tax treaty provisions, if at least one of the following conditions is met for the greater part of the tax year (e.g. for 183 days or more in a calendar year).

- The individual is registered in the Office of Records of the Resident Population in Italy (the "*Anagrafe*").
- The individual has a residence in Italy as defined in the Italian Civil Code.
- The individual has a domicile in Italy, as defined in the Italian Civil Code.

A person's "residence" is their place of habitual abode; their "domicile" is the place they establish as their main centre of business and interests (centre of vital interests).

Meeting at least one of the above conditions is sufficient for an individual to be deemed Italian tax resident.

Spouses are taxed separately on their earned income. Furthermore, each spouse is taxed on half the income of minor children and on half the income generated by (i) jointly-owned marital assets and (ii) family assets.

### 7.1.3 Non-Italian tax residents

Individuals who are not resident in Italy for tax purposes are subject to Italian income tax on certain categories of income from Italian sources only.

Non-resident individuals who:

- are residents of an EU or EEA country that provides for an adequate exchange of information with the Italian tax authorities, and
- derive more than 75 percent of their income from Italian sources

are effectively taxed as Italian residents (including full allowances), subject to the condition that these non-resident individuals do not benefit from similar allowances in their state of residence.

The rule provides for the full recognition of tax allowances and reliefs subject to certain conditions. In particular, qualifying non-resident individuals are required to submit a special declaration in lieu of affidavit

to their withholding agent, providing all the necessary information, e.g. their state of residence for tax purposes and, if they are entitled to personal credits, the personal data of family members. Furthermore, they must keep and, where required, submit various documents to the Italian tax authorities, including a copy of their tax return filed in the foreign state of residence.

# 7.1.4 Types of personal taxes

Taxable income is subject to personal income tax (IRPEF). In addition to IRPEF, regional and municipal taxes are levied, which vary according to the locality of residence in accordance with regulations issued by the regional and municipal authorities.

Moreover, Italian tax resident individuals are subject to wealth taxes (IVIE and IVAFE) on real estate and financial assets held outside Italy.

# 7.2 Taxable income

# 7.2.1 Categories

Resident individuals are subject to individual income tax on their worldwide income, which can be divided into the following categories:

- income from immovable property;
- income from capital;
- · income from self-employment (professional income);
- income from employment;
- business income; and
- miscellaneous income, including capital gains.

The aggregate taxable income is calculated by adding together the income of each category; only losses arising from carrying on a business or exercising an art or profession may be deducted. Tax allowances differ according to the type of income. Losses arising from a business, trade or profession may be carried forward for a maximum of five years and offset against income of the same kind. The profits and losses included in aggregate income are calculated separately for each income category in accordance with statutory rules, based upon the net total of all sources in the same category.

In calculating profits and losses, revenue, expenses and charges in foreign currency are valued at the exchange rate of the date on which they are received or incurred, at the exchange rate of the nearest prior date or, failing that, the average exchange rate of the month in which they are received or incurred.

# 7.2.2 Employment income

### Salary

Income from employment consists of all remuneration, in cash or in kind and including gifts, received during a tax year in connection with employment. All types of pensions and equivalent allowances are deemed to be income from employment.

No deductions for expenses are allowed from employment income.

As a general rule, all reimbursements by the employer are taxable for the employee, with the exception of refunds of travelling expenses, subject to certain terms and conditions.

Payments made upon termination of employment may be taxed separately; however, at the taxpayer's request they can also be taxed under the ordinary taxation system.

# Benefits in kind

As a general rule, benefits in kind are taxable in the hands of the employee if they exceed EUR 258.23 in the tax year. They include benefits received by family members of the employee and benefits from third parties.

Benefits in kind are deemed to constitute income equal to their market value, with some exceptions: special provisions apply, for instance, to vehicles put at the disposal of employees, rental costs for accommodation paid by employers, and low-interest loans to employees from employers.

# Pension income

There are no special provisions for pensions. By law, all pensions and allowances regarded as equivalent to a pension are treated as income from employment. However, certain annuities from qualifying pension plans are treated as income from capital and are, therefore, subject to a substitute tax of 26 percent.

For income deriving from pension funds, the tax treatment differs considerably.

 Periodical payments made by pension funds (TFR payments, contributions made by the employee and deducted or contributions made by the employer and not taxed) are subject to separate taxation at a maximum flat rate of 15 percent. The financial component of annuities is treated as income from capital and subject to a 20 percent substitute tax. Where the fund invests in Italian or white-list country government bonds, the substitute tax is 20 percent but the tax base is

reduced to 62.5 percent.

• The capital component of annuities is not subject to tax.

# Directors' remuneration

Remuneration paid to the members of a board of directors or supervisory board is taxed as employment income. If the functions carried out by a director or supervisory board member are typical of their professional activity, the remuneration is taxed as professional income (see below).

# 7.2.3 Business and professional income

Business income is that derived from running a business. It is generally taxed at the progressive rates of individual income tax. The income of general and limited partnerships, regardless of its source and the purpose of the partnership, is considered to be business income and is calculated in accordance with the rules governing such income. Individuals may opt to have partnership income taxed at the rate of 24 percent (as of 1 January 2017, the corporate tax rate has been decreased from 27.5 percent to 24 percent). Once the income, taxed as such, is distributed to the partners, it is subject to tax at the ordinary progressive rates. Professional income is that derived from a trade or profession and is the difference between the fees received during the tax year (in cash or in kind, including profit shares) and the expenses incurred in practicing that trade or profession during the same period.

# 7.2.4 Investment income

The law lists the items of income that are to be treated as income from capital if received by private individuals (i.e. individuals not engaged in a trade or business). For individual entrepreneurs, these items of income do not constitute income from capital when they relate to their business activity. Instead, they are treated as components of business income and are subject to the rules on calculating such income.

Broadly speaking, in the case of bonds and similar securities, proceeds other than those pre-determined at issue (or indexed) are not regarded as investment income but as miscellaneous income (capital gains) and taxed accordingly.

Investment income includes:

- · interest from loans, deposits and current accounts;
- dividends and other distributions;
- royalties;
- other.

Please refer to section 7.4.2 for the taxation rules on investment income.

# 7.3 Tax-exempt items and personal deductions

# 7.3.1 Tax-exempt income

Payments not treated as taxable remuneration include certain social welfare payments, life and accident insurance payments, and reimbursements of business expenses documented by original receipts.

# Social welfare

Mandatory social security contributions paid by the taxpayer are deductible from taxable income within certain limits and on certain conditions.

Voluntary contributions made to pension funds (i.e. a company's pension fund), even if paid abroad, are tax deductible (or tax-exempt when they are made by the employer) up to the amount of EUR 5,164.57.

# Medical insurance

Contributions of up to EUR 3,615.20, paid into Italian National Health Service funds (*Fondi integrativi al Servizio Sanitario Nazionale*) for medical assistance, both by the employer and by the employee, are not taxable.

# Benefits in kind and reimbursements of business expenses

Reimbursements of business expenses incurred by an employee are not considered taxable remuneration if the expenses can be proven with original receipts.

The following business expenses are not included in taxable income:

- food served in canteens or equivalent services (up to a daily ceiling);
- transportation between home and work, even if this is contracted out to third parties;
- the cost of educational, recreational, health, religious and social welfare services provided by the employer for the benefit of all employees.

If a company car or motorcycle is made available to an employee, the taxable benefit is 50 percent of the amount calculated on the basis of published tables and an assumed annual mileage of 15,000km.

If an employee receives a low-interest loan from his employer or a thirdparty lender, the taxable benefit is 50 percent of the difference between Back to Contents

the official discount rate of interest and the actual rate of interest paid by the employee at the end of each year.

#### 7.3.2 Deductions

Various allowances of differing amounts are granted for dependent family members provided that the family member and taxpayer's income do not exceed certain amounts.

#### Family deductions

The following deductions for family members are allowed as deductions from gross tax. However, deductions only apply if the family member's aggregate annual income does not exceed EUR 2,840.51.

**Dependent spouse** – from zero to EUR 800. This allowance is theoretical as the deduction decreases as income increases. No allowance is granted when income exceeds EUR 80,000.

**Dependent children** – from EUR 950 to EUR 1,220 for children under three years of age with an extra EUR 400 for children with disabilities. If there are more than three children in the family, the amount increases by EUR 200 for each child after the first.

These amounts decrease as income rises. Moreover:

- for taxpayers with one child, the deduction is not available for income of over EUR 95,000.00;
- for taxpayers with two children, the deduction is not available for income of over EUR 110,000.00;
- for three children, the deduction is not available for income of over EUR 125,000.00;
- for four children, the deduction is not available for income of over EUR 140,000.00, and so on.

A further deduction is available for individuals with four or more dependent children who qualify for a deduction. The deduction is EUR 1,200.00, regardless of their income.

The above deductions are also available to non-residents, although the latter must be able to prove their family relationships by means of a local family relationship certificate. They must also:

- generate at least 75 percent of their aggregate income in Italy;
- be living in Italy;
- not benefit from similar deductions in their country of residence.

**Other family members** – EUR 750. This allowance is theoretical and depends on the income amount. No allowance is granted for income above EUR 80,000.

#### Other deductions

Resident taxpayers are allowed to deduct **19 percent** of the following expenses from their gross tax:

- medical expenses exceeding EUR 129.11 incurred by the taxpayer, his/her spouse or other dependents, including fees charged by specialists;
- veterinary expenses: up to EUR 387.34
- voluntary life insurance premiums and accident premiums not exceeding EUR 530.00 (provided that certain conditions are met);
- insurance premiums covering assistance for disabled persons: up to EUR 750.00
- insurance premiums covering self-sufficient risk in everyday life: up to EUR 1,291.14
- interest paid to banks resident in the EU on mortgage loans (on owned-occupied dwellings) secured by property in Italy, up to a maximum of EUR 4,000.00 per year (if other taxpayers share ownership of the property the deduction is calculated in proportion to respective percentages of ownership);
- interest paid to banks resident in the EU on agricultural loans, up to the declared income from the land;
- funeral expenses, up to a maximum of EUR 1,550.00;
- nursery school tuition: up to EUR 632.00
- elementary, junior and high school tuition: up to EUR 564.00
- university fees up to the tuition fee amounts payable to state schools and universities;
- expenses for children's sport activities (for children aged 5 18 years old): up to EUR 210.00 per child;
- expenses paid to real estate agents, up to a maximum of EUR 1,000.00;
- grants for particular public objectives.

Resident taxpayers are allowed to deduct **50 or 65 percent** of the following expenses from their gross tax:

- furniture purchased for a renovated house (50 percent);
- building renovation costs (50 percent);
- energy requalification expenses (65 percent);

The eligible expenses for building renovations are limited to EUR 48,000 per dwelling for building renovations carried out between 2005 and 25 June 2012, and EUR 96,000 for building renovations carried out between 26 June 2012 and 31 December 2017. The deduction for building renovation and energy requalification expenses must be spread over 10 years.

## 7.4 Tax rates

#### 7.4.1 General rules

The following rates of individual income tax apply:

| Taxable income  | Total tax on income<br>below bracket | Rate on excess |
|-----------------|--------------------------------------|----------------|
| EUR             | EUR                                  | Percent        |
| 0 - 15,000      |                                      | 23             |
| 15,001 - 28,000 | 3,450                                | 27             |
| 28,001 - 55,000 | 6,960                                | 38             |
| 55,001 - 75,000 | 17,220                               | 41             |
| Over 75,000     | 25,420                               | 43             |

In addition to personal income tax (IRPEF), regional tax and municipal tax is due on the same taxable income. The tax rates depend on the region and the municipality in which the individual is domiciled. Regional taxes range between 1.23 percent and 3.33 percent, depending on the region. Municipal taxes usually range between 0.0 percent and 0.9 percent.

Up until 31 December 2016, a temporary solidarity surcharge of 3 percent was applied to income over EUR 300,000. This legislation expired on 31 December 2016 and, at the time of publication, had not been renewed.

#### 7.4.2 Separately taxed items

#### Taxation of investment income and capital gains

The tax treatment of both Italian and foreign dividends is summarised below.

Italian dividends

| Recipient  | Non-qualifying<br>shareholding  | Qualifying<br>shareholding                            |
|--|---|---|
| Private individual (dividend taxed as income from capital) | 26 percent final withholding<br>tax on 100 percent of the<br>dividend | Progressive taxation on 49.72 percent of the dividend |

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#### Foreign dividends

| Recipient   | Non-qualifying<br>shareholding   | Qualifying<br>shareholding  |
|---|--|---|
| Private individual (dividend taxed<br>as income from capital) | 26 percent final tax on the dividend net of the tax paid in the foreign country. | Progressive taxation on 49.72<br>percent of the dividend if it<br>derives from a 'white-list'<br>company (100 percent if the<br>shareholding is in a 'black-list'<br>company) |

#### Capital gains

Under Italian tax law, capital gains are treated as miscellaneous income.

The tax is levied on the difference between the selling price and the purchase cost, which may include additional legal and administrative expenses.

The taxation is levied in two different ways.

- Capital gains from the disposal of a non-qualifying shareholding<sup>1</sup>: these are subject to a 26 percent substitute tax to be paid through the income tax return.
- Capital gains from the disposal of a qualifying shareholding<sup>2</sup>: 49.72 percent of the capital gain is taxable at the progressive IRPEF rates.

#### Interest

Generally, interest income is taxable. There are, however, different taxation rules for financial instruments, according to the source of the interest. Interest income from bonds issued by government or similar entities, Italian or foreign (provided that the foreign entities are included in the 'white list') is subject to a final withholding tax of 12.5 percent.

Interest income and income from other securities issued by banks or companies listed on the stock exchange are subject to a final withholding tax of 26 percent. Interest on bank and postal current accounts is subject to a final withholding tax of 26 percent. Taxpayers may choose to tax interest at progressive tax rates.

<sup>1</sup> A 'non-qualifying shareholding' is an equity interest, or equivalent rights to acquire equity, representing less than 20 percent (2 percent in the case of a listed company) of the voting rights that can be exercised at the ordinary shareholders' meeting or less than a 25 percent interest in the capital (5 percent in the case of a listed company). 2 A 'qualifying shareholding' is an equity interest exceeding the thresholds indicated in the above footnote.

#### Royalties

Royalty income includes that derived from the third-party use of intellectual property, patents, industrial inventions, trademarks and know-how. Royalties are treated as professional income if received by an author or inventor, or as miscellaneous income if received by individuals other than the author or inventor. A flat rate of 25 percent of expenses may be deducted from gross royalties where some conditions are met (the deduction is increased to 40 percent if the beneficiary is under 35 years of age).

Payments received from the lease of tangible property are not treated as royalty income but as business income if derived in the course of a trade or business, or as miscellaneous income if derived in some other way.

#### Income from immovable property

In general, income from the ownership of land and buildings is a notional amount based on a cadastral system. In the case of property that is rented out, the taxable basis is the higher of the notional cadastral income and the actual income, net of directly attributable expenses of up to 5 percent of the gross income (i.e. the actual net income cannot be lower than 95 percent of the gross income).

If the immovable property is rented out to an individual for living purposes, the taxpayer may opt for a flat rate tax (*cedolare secca*) of 21 percent (or 10 percent for houses in municipalities with high-density populations) instead of the ordinary progressive tax rates. The taxable base is 100 percent of the rental income according to the rental contract.

Owner-occupied homes are deemed to produce taxable income for the owner. However, the notional income of an owner-occupied dwelling is not subject to tax.

Income from immovable property located abroad is obviously not subject to the cadastral system of taxation.

#### Principal residence: gains and losses

Capital gains realised on the sale of real estate in Italy are generally taxable whether or not the owner is resident in Italy. Italian tax law provides that capital gains realised on the transfer for a consideration of buildings held for less than five years are to be included in the individual's taxable income. The sale of the first habitual dwelling is not taxed as a capital gain if the building has been named as the owner's habitual dwelling for the greater part of the period of possession.

Capital gains realised on the sale of real estate purchased more than five years previously is not taxed.

Capital gains realised on the sale of real estate outside Italy are taxable in Italy under the above rules if the owner is considered to be an Italian tax resident.

#### Taxation of investment capital gains

Capital gains realised on the sale of financial investments are taxable as miscellaneous income. The taxable base is generally the difference between the proceeds and the cost (including the transaction costs).

Since 1 July 2014, the tax rate has stood at 26 percent.

# 7.5 Administrative and filing requirements

#### 7.5.1 Withholding taxes

Salaries and other income from employment paid by companies, businesses and professionals are subject to advance withholding tax, which is creditable against the recipient's income tax liability. The tax is withheld at the ordinary income tax rates corresponding to the relevant brackets, on a pro rata basis according to the period for which the payment is made.

#### 7.5.2 Deadlines

For individual taxpayers, the tax year is the calendar year.

Income tax is generally due by **30 June** of the subsequent year and before the Italian tax return filing deadline; however, the Italian Revenue Office can accept delayed payments with interest and penalties, if applicable. The 730 tax return must be filed by **7 July** of the subsequent year, whereas the filing deadline for the Unico tax return is **30 September.** The RW form is filed together with the Unico tax return.

The deadlines may be extended further by the Italian government.

#### 7.5.3 Foreign asset monitoring

Regardless of their obligation to file an income tax return, all Italian tax resident individuals must comply with exchange control regulations in Italy and consider whether they must also declare their foreign investments.

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Italian tax residents are required to report all assets held outside Italy (on form RW). Such assets include real estate, financial investments, bank accounts, precious metals, artwork, luxury automobiles and yachts. This requirement applies not only to income-producing assets, but also to assets capable of producing future income or gains.

#### 7.5.4 Payment of tax

Income taxes must be paid as described below.

- By 30 June of each year the taxpayer must pay the balance for the previous calendar year and the first advance payment for the current year. The first advance payment amounts to 40 percent of the difference between the net tax amount and withholding taxes and other tax credits. It is possible to pay by 30 July with a small tax surcharge of 0.4 percent.
- By 30 November of each year the taxpayer must pay the second instalment, equal to the remaining 60 percent of the difference between the net tax amount and withholding taxes and other tax credits.

A 30 percent advance payment for the additional municipal income tax must be paid together with the balance of taxes due for the previous year.

#### 7.5.5 Penalties

If the tax return is filed between one and 90 days after the deadline, a penalty of EUR 25.80 is due.

If any tax is due, the following penalties for delayed payments apply (taking payments due in 2017 as an example):

- payment by 31 July 2017 interest of 0.4 percent;
- payment between 31 July and 30 August 2017 if the payment is made between 1 and 15 August 2017, there is a reduced penalty equal to 0.1 percent of the unpaid tax for each day payment is delayed up to and including the payment date, plus interest. Between 16 and 30 August 2017, the penalty is 1.5 percent of the unpaid tax, plus interest;
- payment between 31 August 2017 and 29 October 2017 a reduced penalty of 1.67 percent of the unpaid tax, plus interest;
- higher penalties are due in the event of any further delay in payment.

Tax returns filed more than 90 days after the deadline are considered as omitted tax returns and are subject to penalties of between 120 percent and 240 percent of the tax due. Inaccurate tax returns (which report less taxable income then assessed or higher credits/deductions than assessed) are subject to penalties of between 90 percent and 180 percent of the higher tax due. In some circumstances, criminal penalties may be imposed.

## 7.6 Other taxes

#### 7.6.1 Wealth tax on foreign assets

Foreign financial assets and Italian financial assets held outside Italy are subject to IVAFE. For bank accounts, postal accounts and savings accounts, the tax due is fixed at EUR 34.20 per account. Other foreign financial assets are subject to a tax rate of 0.2 percent of the value at the end of the tax year or at the end of possession, in proportion to the percentage of ownership and days of possession.

Foreign real estate is subject to IVIE. As of the 2016 tax year, if the property in question is used as the principal residence, then IVIE is no longer due (the taxable amount used to be 0.4 percent of its purchase price, in proportion to the percentage of ownership and days of possession). If it is not used as the principal residence, the tax due amounts to 0.76 percent of the purchase price in proportion to the percentage of ownership and days of possession.

#### 7.6.2 Real estate tax

A municipal tax on immovable property (IMU) is levied on those who own immovable property (buildings, development land, rural land) located in Italy.

The taxable base is the notional cadastral income attributed by the immovable property registry, multiplied by 1.05 and then by 160 for residential property.

The tax rate is equal to 0.76 percent (for other buildings not used as the main dwelling). The Municipality may increase or decrease the tax rates. This tax is not deductible for income tax purposes.

#### 7.6.3 Gift and inheritance tax

Gift and inheritance tax is applicable to all Italian residents and also to non-residents who have property in Italy. The tax rates are as follows:

 4 percent for beneficiaries directly related to the donor (i.e. spouse and children) or the bequeather. An exemption is given for the first EUR 1,000,000.00 of assets and cash transferred to each beneficiary;

- 6 percent for siblings of the donor or the bequeather. An exemption is given for the first EUR 100,000.00 of assets and cash transferred to each beneficiary;
- · 6 percent for other relatives, with no tax exemptions;
- 8 percent for beneficiaries not related to the donor or the bequeather, with no tax exemptions.

When real estate is inherited or gifted, cadastral tax and mortgage tax apply at the rates of 1 percent and 2 percent respectively. If the real estate is the principal dwelling, the cadastral and mortgage taxes are substituted by a fixed tax of EUR 200.00.

## 7.7 International aspects

#### 7.7.1 Expatriates

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Income derived by employees from an activity permanently performed abroad is taxable on the basis of notional salaries determined annually by decree of the Ministry of Labour and Social Security (Ministerial Decree of 25 January 2016 for the 2016 tax year) instead of the salary actually received. This applies only if the activity performed abroad is the exclusive object of the employment, is not performed in an occasional way and the employee stays abroad for more than 183 days of the year.

The aforementioned notional salaries are normally used as the basis for paying Italian social security contributions when an Italian employee is seconded to a non-social security treaty country. Italian employers must levy withholding taxes on the monthly notional salary for their Italian employees working abroad and all the benefits linked to the foreign employment are deemed to be included in the notional salary. It may be possible for an Italian employee seconded abroad to be subject to double taxation (in Italy and in the host country). However, double taxation can be avoided or reduced through the tax credit mechanism.

These rules do not apply to Italian employees who are seconded abroad and cease to be Italian tax residents.

#### 7.7.2 Double taxation relief

Resident individuals are subject to individual income tax on their worldwide income. In order to avoid international double taxation, a foreign tax credit is granted to residents with foreign income.

Such foreign taxes may be credited up to the amount of IRPEF due on the same income, based on the ratio of foreign income to total income (net of any tax loss carryforwards).

If foreign income is derived from more than one country, the foreign tax credit is applied separately with respect to each country (i.e. on a per country basis).

The credit must be claimed, upon penalty of forfeiture, in the tax return for the tax year in which the foreign taxes are definitively paid. According to the tax authorities, a tax is definitively paid when no partial or total reimbursement may be obtained.

No credit is granted if an individual fails to file a tax return or report income generated abroad in the tax return. No tax-sparing clause is available at the domestic level.

#### 7.7.3 Specifics of non-resident taxation

Non-resident individuals are subject to individual income tax on Italiansource income. As a general rule, income tax is calculated in the same way as for resident individuals, on the aggregate income derived from Italy.

Non-residents must file an annual tax return for income from Italian sources, as well as income subject to a final withholding tax or to substitute tax. The procedure is the same as for resident individuals.

**Income from employment** (including pensions) is subject to taxation in Italy if the work is performed in Italy. Pensions, similar allowances and termination payments are also subject to taxation in Italy if paid by the state, residents of Italy or Italian permanent establishments of nonresidents.

**Investment income and professional income** are subject to a final withholding tax or substitute tax. Where withholding or a substitute tax is not applied, the non-resident is, when filing a tax return, subject to taxation at the ordinary income tax rates.

**Income from a business** carried on in Italy is only taxable if it is earned through a permanent establishment. Income from a profession practised in Italy by a non-resident is subject to a 30 percent final withholding tax if the payer is a withholding agent. Income from a profession includes directors' fees paid by a resident company.

Non-residents are also subject to IRAP on the net value of production derived from a business or profession run/practised in Italy through a

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permanent establishment or a fixed base for at least three months.

**Dividends** are subject to a final withholding tax of 26 percent unless a lower rate applies under a tax treaty. If tax was also paid on the dividends in the recipient's country of residence, a refund is available up to the percentage provided by the relevant tax treaty.

In general, **interest** payments to non-resident individuals are subject to a final withholding tax at the rates applicable to interest paid to residents. However, a 26 percent rate applies to loan interest paid to individuals resident in a country or territory outside the European Union with a preferential tax regime.

In addition, interest paid to non-residents on deposit accounts with banks and post offices is exempt. Interest paid to non-residents on bonds issued by the state, banks or listed companies with a maturity of at least 18 months is exempt if the beneficial owner is resident in a country with which Italy has an adequate exchange of information. In order to benefit from this exemption, the non-resident must deposit the bonds with a resident bank or other approved intermediary.

**Royalties** paid to non-residents are subject to a 30 percent withholding tax, which is generally applied to 75 percent of the gross payment, resulting in an effective rate of 22.5 percent. However, if the recipient is not the author or the inventor and the underlying right was acquired without consideration, the tax is applied to the full amount of the royalties.

**Income from immovable property** located in Italy is subject to income tax.

**Capital gains** arising from the disposal of immovable property (in Italy) are subject to individual income tax through self-assessment.

As a general rule, capital gains from the sale of shares in Italian companies or other securities are taxable in Italy, unless a double tax treaty applies.

#### 7.7.4 Special tax regime for new non-domiciled residents

The 2017 Budget Law adds article 24-*bis* to the Italian Consolidated Income Tax Code, to provide new residents with a favourable tax regime.

This tax regime allows applicants to pay a fixed tax of EUR 100,000 for themselves and EUR 25,000 for their relatives. The following types of foreign income are eligible:



- rental income;
- capital income;
- employment income;
- self-employment income;
- corporate income (with or without a permanent establishment);
- other income.

The law also offers an exemption from monitoring obligations (RW Form filing) and related wealth tax payments.

Ordinary taxes will only be applied to:

- capital gains from 'qualifying holdings', realised in the first five tax years;
- Italian-source income.

Inheritance and gift tax will be due on Italian assets only (and not on assets held abroad).

The new regime will be available from the 2017 tax year and, once opted for, will run for 15 years. It can be revoked at any time. The special arrangements will terminate immediately if tax is not paid, or is only partially paid, by the tax payment deadline of every year.

The regime is subject to certain conditions:

- foreign tax residence status for at least nine of the previous 10 tax years;
- a favourable tax ruling (the application must be submitted to the tax authorities by the filing deadline for the tax return). This ruling must indicate previous places of tax residence and sources of foreign income.

The practical procedures will be illustrated in a circular to be issued by the Italian tax authorities once the Budget Law enters into force.

#### 7.7.5 Special tax regime for certain inbound expatriates

The Italian Government has decided to offer a tax break to certain workers who move to Italy, by treating 50 percent of their employment or self-employment income as exempt from individual income tax (IRPEF). The exemption runs for five tax years, starting from that in which the worker's residence is transferred to Italy.

The Regime is applicable to individuals:

 a. who have not been resident in Italy in the five tax years preceding the transfer; b. remain resident in Italy for at least two tax years;

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- c. who work for an Italian resident company and have an employment contract with an Italian resident company, a company that controls an Italian resident company, or a company controlled by an Italian resident company directly or indirectly (parent companies);
- d. whose work is carried out mainly in Italy;
- e. who occupy managing or directing roles or are highly qualified/specialised employees.

The same regime also applies to EU citizens and citizens of countries with which Italy has a Double Taxation Treaty or an Information exchange Agreement who have:

- lived abroad continuously for the last 24 months at least;
- have decided to move to Italy after studying, working, or gaining postgraduate qualifications abroad.



# 8. Labour law and immigration

## 8.1 Labour law

#### 8.1.1 Conditions of employment

#### Collective labour agreements

National Collective Labour Agreements (CCNLs – *Contratti collectivi nazionali di lavoro*) between employer associations and trade unions broadly govern employment relationships and the resulting rights and obligations.

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These agreements are the compulsory standard point of reference for employees in particular industries, even if they are not members of a trade union. Case law recognises that CCNLs may establish a minimum salary and minimum terms of employment for each employee; except for in certain cases, an employment contract may not establish working conditions that are less favourable than those defined by the relevant CCNL.

#### Wages and salaries

An employer must pay at least the minimum basic salary established by the relevant CCNL.

The various CCNLs establish a statutory minimum salary for each level of employee; with each periodic renewal of the CCNL there is a salary increase.

An employer can pay additional amounts on top of the minimum basic salary, called "*superminimi*".

An employee's salary is normally paid in 13 monthly instalments (the extra month is paid in December). However, many CCNLs (including the CCNL for the trade sector) also provide for the payment of a 14th instalment, which is generally paid in June. Internal company agreements may provide for even more instalments.

An employer can also grant benefits in kind such as housing, canteen/ subsidised meals, a company car, housing, insurance policies and loans, etc. Both benefits in kind and salaries are subject to taxation and social security contributions.

#### Other conditions

#### Fixed-term or open-ended agreements

Italian labour law allows both fixed-term and open-ended employment contracts.

Legislative Decree no. 81/2015: confirmed that employers are no longer required to justify the use of fixed-term employment contracts.

The maximum duration of a fixed-term contract is 36 months, including extensions. For executives the maximum duration is five years.

The number of fixed-term contracts cannot exceed 20 percent of the number of open-ended contracts in force on 1 January of the same year, unless a different ratio is established by the CCNLs applied by the company.

#### Trial period

The parties may opt for a trial period. The maximum length cannot exceed six months.

A trial period must be agreed in writing before the start of employment; otherwise, the trial period is null and void and the relationship is considered an open-ended employment contract, running from when employment starts.

During the trial period, both the employer and the employee can terminate the employment relationship at any time (without notice and without any indemnity).

#### Working hours

Working hours are established by the law and the CCNLs and cannot normally exceed 40 hours per week for employees.

There is a statutory minimum overtime rate, equal to the ordinary rate plus a certain percentage (approximately 15 percent).

Special rates apply for night work.

#### Holidays

As a general rule, holiday rights cannot be waived.

The holiday allowance is determined by the CCNL for each category of employee and cannot be less than four weeks per year by law. At least two weeks of holiday per year must be taken.

The employer and the employee must agree on the holiday period. Employees are entitled to take at least two weeks of holiday per year during periods of their choice.

#### Maternity leave

There are strict rules on maternity leave and terminating employment relationships with pregnant women, which must be observed very carefully.

Italian labour law provides for compulsory maternity leave. Female employees may not work for two months before and three months after their due date. Alternatively, a woman can decide to stop working one month before her due date and return four months after the birth of her child. In this case, the employee must submit an application to her employer and the National Institute of Social Security (INPS – *Istituto Nazionale della Previdenza Sociale*), with a medical certificate stating that this arrangement will not harm the mother or the child. Back to Contents

Compulsory maternity leave may start earlier or be extended if there are serious health issues or if the employee's job involves tiring duties.

Italian labour law forbids employers from terminating the employment of a pregnant woman from the start of her pregnancy until the child is one year-old. Dismissal is considered null and void in this period.

However, termination of employment during this period is valid under certain exceptional circumstances:

- if there is proof of gross misconduct by the employee, which triggers the immediate termination of the working relationship without any notice period;
- if the company closes;
- if a fixed-term contract expires during this period.

#### Severance pay (TFR - Trattamento di fine rapporto)

Regardless of the circumstances under which an employment relationship ends, the employee is entitled to receive severance pay (TFR – *Trattamento di fine rapporto*), which is approximately equal to their monthly salary multiplied by the number of years of work (re-evaluated each year according to specific accounting rules).

Employers must therefore set aside a TFR provision each year for their employees.

Alternatively, an employee may ask their employer to pay their TFR into a pension fund.

#### Types of employment contract

#### Open-ended contracts

The standard type of employment contract. New open-ended contracts offer various levels of protection against dismissal, which increase the longer the contract remains in force.

#### Apprenticeship contracts

An apprenticeship is an open-ended employment contract aimed at the training and employment of young people.

The contract must be drawn up in writing and contain an individual training plan, following the outlines established by collective bargaining agreements or bilateral agencies.

Unless otherwise provided for by CCNLs, employers with at least 50 workers may recruit new apprentices, provided they permanently take

on at least 20% of the apprentices employed in the 36 months prior to the new intake who have completed their apprenticeship.

#### Occasional work contracts ("Lavoro accessorio")

Contracts allowing for work where total remuneration does not exceed EUR 7,000 per year, paid through "vouchers". If the worker has more than one employer, the remuneration amount paid by each employer cannot exceed EUR 2,000 per year.

#### On-call contracts

Contracts allowed for employees under 24 or over 55 years-old. In any three-year period, the number of days worked cannot exceed 400 (except in the tourism, entertainment, and commercial business sectors).

#### Consultancy agreements

Effective from 1 January 2016, consultancy agreements drawn up on a coordinated and continuing basis are automatically re-classified as employment agreements if the services are personally rendered by the consultant at the principal's premises and if the consultant is bound by working time directives. Exceptions are provided for certain categories identified by CCNLs, individuals enrolled in professional registers (e.g. lawyers, engineers, architects), members of governing and supervisory boards of companies, contractors providing services to sports associations, and companies affiliated with national sports federations.

## Staff leasing and the supply of manpower by employment agencies

Staff leasing contracts can be used in any sector of activity, for up to a maximum of 20 percent of the open-ended contracts in force in the company in question (or up to the limit established by the applicable CCNL). Temporary employees may be supplied only by authorised employment agencies for a limited period of time without justification, within the limits established by the applicable CCNL.

## 8.1.2 The individual and collective termination of employment contracts

### The termination of an individual employment contract - individual dismissals

#### Employees

The dismissal of an employee is valid only when there is **true and just cause** (gross misconduct of the employee resulting in the immediate

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termination of the working relationship without any notice period) or a **justified reason** (less serious misconduct of an employee, or business reasons such as the company's winding-up, reorganisation, etc.). In the case of dismissal for a justified reason, a period of notice must be given.

If the dismissal of an employee is not based on one of the above grounds, and the employee obtains a declaratory judgment of unlawful dismissal, the economic compensation the employee will receive depends on the size of the employer and whether or not the employee was hired before or after the entering into force of the Jobs Act.

In all contracts signed after the entering into force of the Jobs Act, a worker's right to reinstatement is restricted to cases of invalid and discriminatory dismissal. Reinstatement is excluded for dismissals made for business reasons, where compensation (which increases with the length of service) is paid instead.

**Notice period**. When an employee is dismissed for a **justified reason**, the employer must give the employee a period of notice, the length of which is established by the CCNL according to the employee's job title and number of years worked. If there is **true and just cause**, the employment relationship can be terminated immediately.

#### Executives

The rules described above do not apply to executives. CCNLs for executives (which are different for each sector) generally state that there must be good grounds for the dismissal of an executive. Therefore, an executive may contest his dismissal and seek damages if the dismissal is not supported by any valid reason.

**Notice period**. CCNLs for executives specify that the length of the notice period depends on the seniority of the executive.

#### Redundancy procedures - collective dismissals

A collective dismissal is where an employer with more than 15 employees dismisses five employees at least within 120 days.

When a company intends to engage in collective dismissal, it must follow a special redundancy procedure. This procedure also applies when a company is closed down. Law no. 223 of 23 July 1991 establishes the steps to be taken.

- The company must give advance written notice to its internal union representatives and to the trade unions of its intention to start the redundancy procedure
- Written notice must also be sent to the local office of the Ministry of Labour (with a copy of the receipt for the payment made to INPS if applicable) to start the collective dismissal procedure.
- Within seven days of receiving the notice, the trade unions can request a meeting with the company's management in order to

examine the reasons for the decision and evaluate possible alternative solutions. This first phase involving the trade unions ends 45 days after receiving the notice.

- Should the two parties fail to reach an agreement, another attempt must be made by the manager of the local office of the Ministry of Labour. This phase involving the Ministry of Labour ends 30 days after the date of the notice sent by the company to the office informing it of the results of the consultation with the trade unions and the reasons for the negative outcome.
- Once an agreement with the trade unions has been reached, or the procedure has been completed, the company's management must inform the employees of their dismissal in writing, in accordance with the terms and conditions communicated beforehand to the trade unions.

On receipt of their dismissal indemnity, employees normally sign an official settlement agreement at the local office of the Ministry of Labour (*Direzione Territoriale del Lavoro*) or at a trade union office. This is to avoid any future disputes and claims against the company.

The company must also pay the dismissed employees all the other indemnities provided for by Italian law and the relevant CCNL, such as an indemnity in lieu of notice, TFR, additional monthly instalments, and any outstanding holiday leave.

#### 8.1.3 New rules on the posting of workers to Italy

The Italian government recently introduced legislation, i.e. Legislative Decree no. 136/2016, implementing Directive 2014/67/EU concerning the posting of workers in the EU.

The main provisions of the aforementioned Decree are the following:

- when workers are posted to Italy, foreign employers and placement agencies must give **notice** to Italy's Ministry of Labour at least 24 hours in advance, and meet any mandatory obligations provided for by Italian immigration law;
- the home company must appoint a referee in Italy to keep the secondment documentation (employment contract, pay-slips, etc.), which must now be translated into Italian, and a referee to liaise with the trade unions.
- The national labour inspection bodies will verify the authenticity of the secondment by checking and controlling the actual secondment activity and the business relationship between the home and the host company. When a secondment is not genuine (based on the assessment), the posted workers are considered as being directly hired by the host company; furthermore, both the home and host company will be subject to sanctions in such an event.

- Workers seconded to Italy must be granted the same treatment (both economic and regulatory) as other workers of the same level and with the same duties hired in Italy.
- The home and host companies are jointly liable with regard to the treatment of workers.

#### 8.1.4 The social security and pension system in Italy

## The social security system (accident coverage, unemployment, sickness, maternity)

A state-run system of social security operates in Italy, covering illness, maternity, unemployment, pensions, disability and family allowances. This system is financed by contributions from employees and employers, calculated as a percentage of the employee's gross remuneration.

As these contributions represent a relatively high surcharge on employment costs, they are of paramount importance in determining operational business costs.

The employer's share of social security contributions ranges from 29 to 32 percent of the employee's gross salary, while the employee contributes approximately 10 percent. Similar percentages apply to executives, although contributions can be made through various types of specialised funds.

The employer must also pay contributions to the National Institute for Accidents at Work (INAIL), to cover the risk of accidents at work or occupational diseases. The cost of this insurance ranges from 0.4 to 3 percent of the employee's gross salary.

#### Pension treatment

Italian law provides for two different types of pension: old-age pensions and seniority pensions.

#### Old-age pensions

Employees registered with INPS are entitled to an old-age pension provided that they meet the following requirements:

- they have paid social security contributions for at least 20 years;
- they are 66 years and seven months old (men) or 65 years and seven months old (women) – as of 2017, but the required age will increase in years to come, also taking into account the increase in life expectancy.

The right to an old-age pension is subject to termination of employment.

#### Seniority pensions

Employees registered with INPS are entitled to a seniority pension when they meet one of the following requirements;

- they have paid contributions for 42 years and 10 months (men);
- they have paid contributions for 41 years and 10 months (women).

This requirement increases gradually up to 45 years of seniority contributions.

## 8.2 Immigration

#### 8.2.1 EU citizens

Entry requirements, immigration procedures and working activities are regulated by the Schengen Agreement, which made it possible to build a common area of free movement between the signatory states and eliminate border controls. EU citizens with a regular passport/ID card can travel in Italy and are exempt from entry/visa requirements.

#### Residence

EU citizens may reside in Italy for fewer than 90 days without having to register at the town hall. If an individual remains in Italy for more than three months, registration is necessary.

#### Employment

EU citizens are free to work in Italy without requiring any special work permit.

#### 8.2.2 Non-EU citizens

#### Entry for business/tourism

A non-EU citizen must have an entry visa in their passport to enter Italy. However, some foreign citizens entering Italy – such as Japanese or American citizens – do not require a visa for tourism or business trips, provided that they do not stay for more than 90 days. In other cases, entry visas are issued by Italian consulates in the country of origin or last residence. This kind of visa does not allow the person to work permanently in Italy.

#### Entry for study

A visa for study purposes may be requested at the Italian consulate in the foreigner's country of residence. It is valid for the length of the student's course, but cannot exceed one year. A foreign national who legally enters Italy for an intended stay of more than 90 days must apply for a permit to stay within eight working days of their arrival.

The application for a permit to stay must be submitted by post.

The permit to stay will indicate the same reasons for the stay as those stated in the entry visa.

The permit to stay for study purposes also allows the person in question to have a part-time job.

#### Entry for family reunification purposes

This type of visa is granted when the applicant is a foreigner already residing in Italy and holds a residence card or permit to stay that is valid for no less than one year and is issued for employment purposes (including self-employment), study or for religious reasons. The visa will only be granted to the applicant's immediate relatives, such as a spouse or children. This type of visa allows the holder to work.

#### Entry for work

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To work in Italy, a foreign national must hold a work visa. There are limits on the number of foreign citizens that can be hired in Italy each year.

However, the secondment of workers is generally excluded from the limits established by the Italian government, given that it involves companies engaging highly qualified workers.

The main requirement for secondment is a relationship between the home company and the host company in Italy. Nevertheless, a work visa is still required for a seconded worker. The company to which the worker will be seconded must submit an application to its local branch of the Immigration Office (*Prefettura Sportello Unico per l'Immigrazione*). The Immigration Office checks the working conditions and the documentation required and then issues the work visa, along with a certificate of no impediment (*Nulla Osta*). The working conditions cannot be less favourable than those established by the relevant CCNL.

Once the *Nulla Osta* has been obtained, the foreign worker must obtain a visa from the Italian diplomatic mission in their country of residence.

A foreign national who legally enters Italy for an intended stay of more than 90 days must apply for a permit to stay within eight working days of their arrival. Within this same period, the worker and the Italian employer must sign a 'stay contract' summarising the main employment conditions.

The application for a permit to stay must be submitted by post.

The permit to stay will indicate the same reasons for the stay as those stated in the entry visa.



# 9. VAT

## 9.1 Scope

VAT is due on any taxable supply of goods or services made in Italy by a taxable person in the course of or to further their business. Supply means all forms of supply, but does not normally include anything done for anything other than a consideration. However, certain transactions without consideration are deemed to be supplies, e.g. conditional sales, lease contracts with a binding clause providing for the transfer of ownership, the private use of business assets (or, more generally, their use for purposes other than those of the business), free-of-charge disposals, and supplies of services (where the value exceeds EUR 50) for private use or for free.

VAT is also due on all imports.

## 9.2 Rates

The standard rate of VAT is 22 percent.

There is a reduced rate of 10 percent for some goods and services, including:

- · certain foods;
- domestic fuel and power;



- public transport;
- · certain pharmaceutical products;
- water;
- hotel accommodation;
- the services of writers and composers;
- social housing;
- power derived from renewable sources.

In addition, there is a reduced rate of 4 percent for certain goods and services, including:

- basic foodstuffs;
- books, newspapers and e-books;
- a person's main dwelling;
- certain pharmaceutical products;
- medical equipment and aids for the disabled.

The list of zero-rated supplies includes:

- exports and EU supplies;
- the supply, modification, repair, maintenance, chartering and hiring of sea-going vessels and aircraft used for international traffic;
- international transport services;
- services directly connected with exports or imports;
- work on goods to be delivered outside Italy.

The list of exemptions includes:

- finance;
- insurance;
- tax collection transactions;
- lotteries, betting, and other games of chance;
- certain transactions involving residential property;
- postal services;
- cultural services;
- certain real-estate transactions.

NB: It is not possible to recover VAT on exempt supplies.

The 2017 Budget Law provides for a gradual increase in VAT rates starting from 1 January 2018, as follows:

- the reduced 10 percent VAT rate will increase by three points (from 10 percent to 13 percent) on 1 January 2018;
- the standard VAT rate will increase:
  - from 22 percent to 25 percent on 1 January 2018;
  - from 25 percent to 25.9 percent on 1 January 2019;
- the 'super' reduced VAT rate of 4 percent will remain unchanged.

These VAT rate increases will not apply if certain budgetary targets are met.

It also introduced a new VAT rate of 5 percent into the Italian VAT Act.

Medical and social services, educational, home care, outpatient, community services and the like provided by cooperative companies and their consortia, are subject to this new reduced VAT rate of 5 percent (instead of the previous 4 percent rate).

## 9.3 Registration

#### 9.3.1 Italian entities

If a business makes taxable supplies in Italy, it is required to register for and account for Italian VAT. There is no VAT registration threshold in Italy.

#### 9.3.2 Non-Italian entities

The registration rules that apply to Italian entities also apply to non-Italian entities making taxable supplies in Italy (that are not subject to the reverse charge mechanism).

If a business is not registered for VAT in Italy and sells and delivers goods from another EU Member State to customers in Italy who are not VAT-registered (distance sales), it is required to register and account for VAT in Italy (through the direct identification procedure, where possible, or by appointing a VAT representative) when the value of these sales exceeds EUR 35,000.00.

The direct identification form and instructions, as well as the form and instructions for appointing a VAT representative, can be found on the Italian tax authorities' website:

#### www.agenziaentrate.it

The penalty for failing to register for VAT on time ranges from EUR 500.00 to EUR 2000.00.

Certain simplification schemes may apply as follows:

Triangulation

If a business in one Member State (acting as an intermediate supplier to an Italian buyer) purchases goods from a business in a second EU Member State and the goods are then delivered directly from that second Member State to Italy, VAT can be accounted for by the Italian customer (if registered as a VAT person).

Call-off stock
 When a foreign company stores stock at the Italian customer's

premises and the goods remain under its control, the customer will account for VAT on the supply as an acquisition at the moment in which it removes the goods from the premises.

· Supply and installation

If a business supplies goods and installs or assembles them in Italy, its customer must account for acquisition tax. The business must be registered for VAT in another EU Member State and the goods must be shipped from within the EU.

• Domestic reverse charge

In general, the obligation to account for VAT due can be shifted to the customer (if the supplier is a non-established entity), provided that the latter is established in Italy and registered for Italian VAT purposes, and that the supplier does not have an Italian fixed establishment intervening in the supply. These provisions are subject to particular requirements. In compliance with article 17(2) of the Italian VAT Act (implementing articles 194 and 196 of the VAT Directive), customers established and VAT-registered in Italy are liable to account for Italian VAT under the compulsory reverse charge mechanism with regard to domestic supplies of goods and services carried out by suppliers established in other Member States; for this purpose, customers must supplement the invoices issued by their suppliers with the proper Italian VAT rate and Italian VAT amount to be paid. For domestic supplies of goods and services from non-EU suppliers. Italian customers are required to issue a new document, a "self-invoice", charging Italian VAT to themselves.

## 9.4 VAT grouping

The 2017 Budget Law introduced new VAT grouping rules in Italy, effective from 1 January 2018. VAT group members must be taxable persons (not necessarily companies) established in Italy. Permanent establishments located abroad are not eligible to join. Companies that are in the process of being wound up or are subject to bankruptcy or asset seizure procedures by the courts are excluded.

To join a VAT group, taxable persons must have financial, economic and organisational links.

- The financial link is one of control, and must have existed since 1 July of the calendar year preceding the one in which the option is exercised (the minimum holding period). The person with control must be an Italian resident or be based in a country that has an exchange of information agreement with Italy.
- The economic link is activity-based. All members must have the

same core business, or their activities must be complementary/ interdependent or benefit the other members in some way.

The organisational link is one of legal coordination between the decision-makers.

That said, if a financial link exists, the other links are presumed to exist unless an application for a ruling from the authorities stating that they do not exist is submitted.

A group is set up by all the taxable persons who are established in Italy and have the necessary links (according to the 'all-in, all-out principle') with the relevant option being exercised electronically by the representative member of the group. The timing of this determines the start date of the group. If the option is exercised between October and December, the group will not exist until the start of the second year thereafter. So an option exercised in October 2018 would lead to the group only being effective from January 2020, whereas an option exercised on 30 September 2018 would lead to the group becoming effective in January 2019. New members can join once they meet the necessary conditions.

Failure to exercise the option by one or more persons in the VAT group leads to the tax benefit of the group being clawed back and the group ceasing to exist starting from the year following that in which the failure to exercise the option takes place, unless the aforementioned persons subsequently exercise the option to join the group.

The option is binding for three years and automatically renewed annually thereafter until revoked. If one member revokes the option, the whole group is dissolved. Again, the timing of the revocation determines the date on which the group is dissolved in the same way that the timing of the exercising of the option determines the start date. Any member that ceases to have the necessary links, or to meet the other necessary conditions, shall cease to be a member.

The representative member of the group is the controlling member or, if the controlling person is not in the group, the one with the highest turnover or revenue.

The representative has the biggest responsibility for ensuring compliance, but all the members are jointly and severally liable for VAT debts.

Intra-group transactions are not treated as supplies. External sales and purchases are those made by and to the group.

The special simplified compliance obligations for banks, insurance companies and fund managers apply even when they belong to a VAT group.

The other consolidated VAT regime provided for by article 73 of the Italian VAT Act remains in force as an alternative to the VAT group regime.

Under the consolidated VAT regime provided for by article 73 of the Italian VAT Act, members may consolidate their VAT position to offset their respective VAT debts and credits. Thus, the payment and repayment positions of the companies in a consolidated group may be pooled even if each group member has its own VAT number. When this happens, intragroup transactions are not disregarded in Italy, because the members remain separate VAT persons.

VAT repayment positions accrued by new consolidated VAT group members before they enter the group cannot be used to offset the net VAT payment positions of other members.

However, some changes have been introduced by the 2017 Budget Law.

For the 2017 financial year, the option for the consolidated VAT regime should be exercised in the Vat Group section of the annual VAT return (i.e. not in a separate form). The option should be exercised in the VAT return submitted in the financial year in which the consolidated VAT regime should start (e.g. the option for the 2017 financial year should be exercised in the annual VAT return for the 2016 financial year, which should be submitted by the end of February 2017).

Moreover, the minimum holding period for this regime should be observed starting from 1 July of the calendar year preceding the one in which the option is exercised (i.e. not from the beginning of the calendar year preceding the one in which the option is exercised).

## 9.5 Returns

All registered businesses are required to submit VAT returns annually. VAT is paid on a monthly or quarterly basis and repayments are made on an annual basis (quarterly repayment claims are admitted in certain cases).

Annual VAT returns for the 2017 financial year onwards must be filed between 1 February and 30 April of the following year. The deadline for the annual VAT return for the 2016 financial year is the end of February 2017.

Failure to file VAT returns and settle any outstanding payments on time may result in penalties of up to 240 percent of the outstanding amount of VAT.

New VAT reporting obligations as of 2017 include: (i) the quarterly communication of data in invoices received and issued, and (ii) the quarterly communication of periodical VAT settlements, both due by the end of the second month following the relevant quarter. For the 2017 financial year only, invoice data for the first and second quarters will be due by 25 July 2017.

In Italy, the European Sales Listings (ESL) and statistical report forms (Intrastat) have been combined. They are normally referred to collectively as Intrastat returns. There is a separate return for outbound supplies, for both goods and services. The Intrastat form for inbound supplies, for both goods and services, will be abolished as from 2018.

Intrastat returns may be submitted on a monthly or quarterly basis, depending on levels of EU supplies over the previous four quarters.

Monthly returns should be submitted where supplies have been equal to or exceeded EUR 50,000.00 in each of the four previous quarters. The thresholds are calculated for inbound and outbound supplies separately.

Failure to submit Intrastat returns on time may result in a penalty ranging from EUR 500.00 to EUR 1000.00, plus an additional penalty (for statistical violations) ranging from EUR 500.00 to EUR 5000.00.

The Intrastat forms can be found on the following website:

#### www.agenziadogane.it

## 9.6 VAT recovery

Non-registered persons established outside Italy can recover Italian VAT if the amount is over or equal to EUR 50.00.

Under EU procedures in place since 2010, a claimant established in another EU Member State should file an electronic claim with the authorities of its Member State of residence. A non-EU business should recover VAT under the 13th Directive (the refund is conditional upon the non-EU state granting comparable turnover tax advantages; currently, only the Norwegians, Swiss and Israelis can submit such claims).

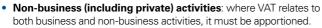
There are strict conditions and deadlines for making claims. The claim period follows the calendar year and claims must be submitted by 30 September of the following year. The claim period can be shorter than a calendar year (a quarter) if the amount of VAT recoverable in that period is over or equal to EUR 400.00.

The 13th Directive claim forms can be found on the Italian tax authorities' website:

#### www.agenziaentrate.it

There are certain items on which VAT cannot be recovered or on which it is only partially recoverable. Some examples are given below:

• **Exempt supplies**: where VAT relates to both taxable and exempt supplies, it must be apportioned.



 Vehicles (excluding commercial vehicles): the VAT recovery rate is limited to 40 percent for expenditure on cars not wholly used for business purposes. The limit covers any expenditure on cars: the purchase of the vehicle (including assembly contracts and the like), intra-Community purchases, imports, leasing or hire, modifications, repair or maintenance, lubricants, fuel, etc.

The restriction does not apply if the vehicle falls into any of the following categories:

- the vehicle forms part of the taxable person's stock in trade in the exercise of his activity;
- the vehicle is used as a taxi;

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- the vehicle is used for instruction by a driving school;
- the vehicle is hired or leased out;
- the vehicle is used by sales representatives;
- Business entertainment: VAT is generally not recoverable on business entertainment costs.
- Tour operators' margin scheme: VAT cannot be reclaimed for goods and services supplied under this scheme.
- Goods sold under one of the margin schemes for second-hand goods: there are a number of schemes under which VAT is accounted for on the sales margin of the goods but cannot be recovered on the purchase of those goods.

# 9.7 International supplies of goods and services

#### 9.7.1 Exports

#### Goods

If a seller in Italy sells goods to a customer who is registered for VAT in another EU Member State, and the sale involves removing those goods from Italy (by the seller or the customer) and sending them to that Member State, then the seller does not charge VAT and zero-rates the supply as an intra-EU supply. The seller must obtain the customer's VAT number in the other EU Member State and quote it on the invoice. The seller should also obtain evidence of the removal of the goods from Italy. If goods are sold to a customer who is not registered for VAT in another EU Member State, the seller will have to charge Italian VAT. If the seller exports goods to a customer (business or private) outside the EU, then it does not charge VAT; however, as with intra-Community sales, the seller should make sure that in all cases it keeps proof of dispatch/ delivery to support its zero-rating.

Please also remember that with the entry into force of the Union Customs Code, on 1 May 2016 the definition of "exporter" changed. In particular, according to article 1(19) of EU Regulation No. 2015/2446, an "exporter" is "the person established in the customs territory of the Union who, at the time when the declaration is accepted, holds the contract with the consignee in the third country and has the power for determining that the goods are to be brought to a destination outside the customs territory of the Union". Please refer to the Customs section for further details.

#### Services

If a supplier established in Italy provides services to a business customer established in another EU Member State or outside the EU, they make a supply that is outside the scope of Italian VAT. In order for the supplier not to charge VAT, the customer in the other EU Member State must have a VAT number, which must be quoted on the invoice.

The following services are subject to different 'place of supply' rules:

- services connected with immovable property please note that the interpretation of services connected with immovable property according to Implementing Regulation (EU) No. 1042/2013 should apply as of 1 January 2017
- passenger transport;
- restaurant and catering services;
- short-term hiring or leasing of means of transport;
- admissions and services ancillary to admissions to cultural, artistic, sporting, scientific, educational, entertainment, or similar activities.

#### Habitual exporters

A resident company acquires the status of habitual exporter if it makes zero-rated supplies (exports, EU supplies, international services, etc.) that account for more than 10 percent of its total turnover.

A habitual exporter is entitled to purchase VAT-free services and goods (exceptions apply for immovable property and goods and services on which VAT cannot be recovered) up to the amount of the zero-rated supplies made in the previous calendar year or previous 12 months. Documentation obligations and procedures apply: in order to benefit from VAT-free treatment, the habitual exporter must send the Italian tax authorities a 'declaration of intent' form and, after obtaining a receipt of transmission, must provide its supplier with both the declaration of intent form and the receipt of transmission.



A new format of the letter of intent should be used for transactions carried out as of 1 March 2017.

The return and instructions can be found on the following website:

#### www.agenziaentrate.it

#### 9.7.2 Imports

When goods are imported into Italy from outside the EU, import VAT and customs duties may be due. These must be paid or guaranteed before the goods can be released by customs control authorities.

If certain services are bought in from outside Italy, the reverse charge mechanism must be applied. This is intended to eliminate any VAT advantage in buying those services from outside Italy.

Under the reverse charge mechanism, it is necessary to account for a notional amount of VAT as output tax in the VAT return covering the period in which the payment is made. This VAT is recovered as input tax in the same return.

If all of the VAT can be recovered, the reverse charge has no cost effect and is a VAT compliance matter only. However, if there is a partial exemption there is likely to be a VAT cost, depending on the level of recovery allowed under the partial exemption method.

## 9.8 Invoices

An invoice should contain the following details:

- the date of issue;
- a progressive number that "univocally identifies the invoice" (since
  1 January 2013 the VAT Law has ceased to require progressive
  numbering according to calendar year). If the invoice adjusts an earlier
  invoice (like a credit note, for example), unambiguous reference
  should be made to the original invoice, the supplier's VAT number, the
  customer's VAT number (if this is a taxable person) or tax code (if this is
  a private individual), and in cases involving a taxable person established
  in another Member State of the European Union, the VAT identification
  number issued by the Member State of establishment;
- the company name, the name and surname, residence or domicile of the supplier and tax representative, as well as the location of the permanent establishment for non-resident persons (if any);
- the company name, name and surname, residence or domicile of the purchaser and tax representative, as well as the location of the permanent establishment for non-resident persons (if any);

- the quantity, quality and nature of the goods/services supplied;
- the tax base according to the applicable VAT rates;
- the unit price (exclusive of any VAT);
- the market value of goods sold at a discount, whether or not this value is included in the calculation of the taxable amount;
- the rate, amount of tax due and tax base rounded up to the nearest Euro cent along with an indication of the person who issued the invoice (for self-invoicing).
- for transactions that are not subject to VAT, in the place of VAT due, the following annotations should be included:
  - "inversione contabile" ("reverse-charge"), for supplies of goods and services subject to the reverse charge mechanism, when the customer is VAT-registered in another Member State;
  - "operazione non soggetta", for supplies of goods and services for which the place of supply is outside EC territory;
  - "autofatturazione" ("self-invoicing"), for invoices issued by the buyer of a good or the recipient of a service when this person is liable to pay VAT;

When the amount of the invoice is no higher than EUR 100 (although the threshold could be extended to EUR 400 by a future Ministerial Decree), or when a credit note is issued in compliance with article 26 of the Italian VAT Act, a simplified invoice may be issued. A simplified invoice is not allowed in the following cases:

- for intra-community supplies pursuant to article 41 of Law Decree no. 331/93;
- for supplies whose place of supply is outside Italian territory and which are subject to reverse charge in another Member State.

According to article 21(1) of the Italian VAT Act, e-invoices are those "issued and received in any electronic format; the use of electronic invoicing is subject to the consent of the customer".

The issuer of the invoice should ensure the authenticity of the origin, the integrity of the content and the readability of the invoice from the moment of issue up until the end of the retention period.

The authenticity of the origin and integrity of the content may alternatively be guaranteed through:

- business controls that create a reliable audit trail between the invoice and the related supply of goods or services, or
- the use of qualified or digital electronic signatures by the issuer, or
- EDI data transmission systems, or
- other technologies (chosen at the taxpayer's discretion) that can guarantee the authenticity of the origin and the integrity of the data.

Electronic invoicing is compulsory for supplies to public authorities and administrations (PA). Since 1 January 2015, sales to PA have fallen under

a special regime called "split payment", under which suppliers continue to charge Italian VAT (where due, and unless the reverse charge mechanism applies) to public bodies. The public bodies, however, 'split' the payment of the invoice: they pay the taxable amount to the suppliers, and the VAT to a blocked VAT bank account of the Treasury.

A Ministerial Decree issued on 23 January 2015 clarified the payment procedure, including the conditions and time frames involved.

Self-invoicing is allowed. However, the supplier remains responsible for issuing the invoice. Furthermore, if the issuer is resident in a 'black-list' state, the supplier (who must have been in business for at least five years and must not have undergone a VAT assessment by the tax authorities in the previous five years) must notify the tax authorities of the arrangement beforehand.

## 9.9 Transfers of business

If a business is sold as a going concern then VAT is not due. The transaction is subject to registration tax and certain conditions must be satisfied; for example, the purchaser must intend to use the assets to carry on the same kind of business carried on by the seller.

## 9.10 Opting for VAT

Italian VAT law grants a general exemption for real estate transactions, with certain exceptions. However, in the case of industrial real estate, it is possible to opt – in the transfer deed – for the transaction to be taxed. In the same way, it is possible to opt for taxation, on a unit-by-unit basis, of leased industrial real estate. Again, this form of taxation must be opted for in the leasing agreement.

The reverse charge procedure applies to the transfer of industrial real estate if the supplier has opted to pay VAT.

## 9.11 Head office and branch transactions

From a VAT perspective, for sales of goods, the local branch and the foreign head office are treated as separate entities, so no transactions are disregarded.

As regards services, in light of the judgment in the FCE case before the European Court of Justice (C-210/04), the Italian tax authorities have clarified that services provided between a head office and its branch are disregarded for VAT purposes (on the condition – as pointed out by ECJ judges – that the branch has no decisional autonomy).

The Italian tax authorities have not issued any official guidelines to clarify the possible impact of the Skandia case on the head office and branch exemption.

## 9.12 Bad debts

VAT relief can be claimed for bad debts in principle if they are due to a customer's bankruptcy or insolvency (when foreclosure procedures are unsuccessful).

The 2016 Budget Law made it possible to claim Bad Debt VAT relief at the beginning of the procedure (instead of waiting until the end). This provision should have applied to bankruptcy and similar procedures declared after 31 December 2016.

However, the 2017 Budget Law repealed the changes introduced by the 2016 Budget Law, which never came into effect (the 2017 Budget Law cancelling the 2016 changes entered into force on 1 January 2017).

So like in the past, output VAT unpaid by customers under bankruptcy and similar procedures is recoverable only <u>at the end</u> of the procedure.

According to article 26(12) of the Italian VAT Act, a foreclosure procedure is deemed as having been unsuccessful when:

- a. if ordered, a third party seizure cannot be carried out due to an absence of assets or credits to seize;
- b. if ordered, a seizure of moveable goods cannot be carried out because goods are missing or because the debtor cannot be found;
- c. after three attempts to sell the goods at public auction with no success, the foreclosure procedure is interrupted due to excessive costs.

## 9.13 Anti-avoidance

In effect since October 2015 is a general "abuse of law" rule, which also applies to VAT. Please refer to section 5.1.11 for more information.

In addition to this general rule, a rule to combat missing trader intra-

Community fraud, also known as carousel fraud, in Italy establishes that the purchaser has joint liability for VAT not paid by the seller. This anti-fraud rule only applies to a limited series of goods (cars, motorcycles, mobile phones, computers, new and used pneumatics and flaps, livestock, and fresh meat), and is only triggered when the good's price is lower than the market value.

Specific anti-avoidance provisions exist whereby the fair market value becomes the tax basis in certain transactions between related parties that are partially exempt.

VAT payers used to be required, on an annual basis, to report supplies of goods and services worth over EUR 10,000 made to and by their trading counterparts in 'black-list' countries. Starting from the financial year ongoing on 31 December 2016, reports of transactions with trading counterparts in 'black-list' countries ('black-list reports') will no longer be due.

## 9.14 Penalty regime

The VAT penalty regime can be categorised according to the type of violation committed by the taxpayer, as described below.

Decree no. 158/2015, published in the Italian Official Gazette on 7 October 2015, amended some of the below administrative penalties with effect from 1 January 2016.

#### Violations connected with the VAT return

**Failure to submit an annual VAT return**: the penalty ranges from 120 to 240 percent of the amount that should have been declared in the return. If VAT is not due on any of the taxpayer's transactions, the penalty ranges from EUR 250.00 to EUR 2,000.00.

**Submission of an inaccurate VAT return**: the penalty ranges from 90 to 180 percent of the VAT not shown or of the excess VAT credit declared.

#### Failure to record transactions

Failure to record transactions subject to VAT (including EU acquisitions): the penalty ranges from 90 to 180 percent of the VAT due.

Failure to record transactions that are VAT-exempt or non-taxable:

the penalty ranges from 5 to 10 percent of the unrecorded amount. The same penalty also applies in the event of the failure to invoice certain "outof-scope" transactions. The penalty cannot be lower than EUR 500.00 per violation. Failure to record VAT-exempt or non-taxable transactions, which does not result in corporate income tax violations: the penalty ranges from EUR 250.00 to EUR 2,000.00.

Where the supplier of goods or services fails to issue an invoice, or the invoice contains a mistake, the purchaser is subject to a penalty equal to 100 percent of the related VAT if he fails to put the (non-issued or incorrect) invoice in order. Doing so involves specific formalities.

There are reduced penalties for violations of domestic reverse charge procedures, when VAT has actually been paid by one of the parties. In this case, the penalty ranges from EUR 250.00 to EUR 10,000.00.

#### Violations connected with exports

Penalties apply when a taxpayer does not comply with various provisions allowing VAT to be collected on exports. In principle, the penalties are proportional to the amount of VAT that could potentially be collected.

#### Other violations

There are fixed penalties for taxpayers who commit violations such as submitting a VAT return that does not comply with the official format, failing to submit certain VAT communications, or failing to keep VAT records. The size of the penalty depends on the type of violation.

#### Failure to make payments / making underpayments

The penalty is 30 percent of the unpaid amount, plus interest of 4 percent on the unpaid amount.

It is a criminal offence to fail to pay the VAT declared in an annual tax return by the deadline for the advance payment of the following year. This rule is triggered if the amount of VAT is higher than EUR 250,000.00 (The taxpayer can be given a prison sentence ranging from six months to two years.

The same applies to taxpayers who offset inexistent or undue VAT credits against tax payments for an amount higher than EUR 50,000.00 per year.

#### General rules

Where the law imposes a range of penalties, the actual amount is established by the tax authorities at the time of assessment.

When determining the amount, the tax authorities consider the severity of the violation, in light of the taxpayer's behaviour and social and economic situation.



The penalties may be increased by 50 percent if the taxpayer has committed similar violations that have been declared final in the last three years.

In an assessment, each violation committed by the taxpayer should trigger the corresponding penalty. However, there are mechanisms for calculating the penalties more leniently if the same violation is committed more than once in a tax year or over several years.

In addition to fines, there are other penalties such as the suspension of trading licences.

#### Voluntary disclosure and amendment

The taxpayer can reduce the above penalties (i.e. the penalties that would be due following an ordinary assessment) through voluntary disclosure and amendments (*ravvedimento operoso*) by a given deadline.



# 10. Customs and excise and import VAT

## 10.1 European Community law and the customs system

Customs law is the best example of harmonised international tax law.

In Italian as in international customs law, there are three fundamental concepts.

- The classification of goods. This is necessary in order to select and apply the relevant customs rules for each movement of goods and thus to quote the import duty;
- The origin of goods. For customs purposes, the origin of goods can be preferential or non-preferential ('made in' labelling);
- 3. The value of the transactions. According to article 70 of the Union Customs Code (the "UCC" – Regulation (EU) No. 952/2013 of the European Parliament and of the Council), "the primary basis for the customs value of goods shall be the transaction value, that is the price actually paid or payable for the goods when sold for export to the customs territory of the Union, adjusted, where necessary".

The current framework of customs law is a complex structure of national and Community rules, which accumulated as the European integration process developed.

## 10.2 Customs declarations

Community law stipulates that all goods intended to be placed under a customs procedure must be governed by a declaration for that procedure. The declarant indicates a wish to place goods originating in third countries under a given customs procedure and provides information about the transaction. For each product, the declarant must indicate the classification code, origin, value, quantity, consignor and consignee, and the customs procedure.

This basic information enables the customs authorities to determine the dutiable amount and must be supplemented with other information about the transaction concerned.

#### The Union Customs Code

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The Union Customs Code (UCC) was adopted on 9 October 2013 by way of Regulation (EU) No. 952/2013 of the European Parliament and of the Council, and repealed the Community Customs Code (the "CCC" – Council Regulation (EEC) No. 2913/92).

It entered into force definitively on 1 May 2016, once the UCC-related Commission acts (delegated and implementing acts) were adopted and entered into force.

The UCC is part of the modernisation of customs, and is the new framework regulation on customs rules and procedures throughout the EU.



The UCC and the related delegated and implementing acts:

- streamline customs legislation and procedures;
- offer greater legal certainty and uniformity to businesses;
- increase clarity for customs officials throughout the EU;
- simplify customs rules and procedures and facilitate more efficient customs transactions in line with modern-day needs;
- complete the shift by Customs to a paperless and fully electronic environment;
- reinforce swifter customs procedures for compliant and trustworthy economic operators (Authorised Economic Operators).

With the introduction of the UCC, Community law now requires the paperless exchanges of information between different authorities and between authorities and economic operators, stipulating that all data exchanges must take place using electronic data-processing techniques.

This innovation, among others introduced by the Automated Export System (AES), marks a paradigm shift in customs law, making electronic data exchange the key factor in the relationship between companies and customs authorities.

Article 14(2) of the UCC stipulates that customs authorities must maintain a regular dialogue with economic operators. The same authorities must promote transparency by making information about customs law, general administrative rulings and application forms available to the public – free of charge whenever possible.

The provision adds that this objective may be pursued via the Internet. This is further proof of the total modernisation of customs regulations through the UCC, which also provides for 'institutional' exchanges via the Internet, with full legal recognition and no exceptions.

Moreover, article 16 of the UCC states that "Member States shall cooperate with the Commission to develop, maintain and use electronic systems for the exchange of information between customs authorities and with the Commission and for the storage of such information, in accordance with the Code".

#### **10.2.1 Suspensive arrangements and customs procedures** with economic impact (special procedures under the UCC)

Under the new UCC, the suspensive customs procedures laid down in the repealed CCC are replaced by the following "special procedures":

- a. transit, which comprises external and internal transit;
- b. storage, which comprises customs warehousing and free zones;

- c. specific use, which comprises temporary admission and end-use;
- d. processing, which comprises inward and outward processing.

It should be noted that the "Processing under customs control" procedure has been included in the new inward processing procedure, "temporary admission" is covered by the new "specific use" procedure, and "free zones" are now governed by "customs warehousing" rules.

#### Transit

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#### External transit

Under the external transit procedure, non-Union goods may be moved from one point to another within the customs territory of the Union without being subject to *i*) import duties, *ii*) other charges provided for under other relevant provisions in force, or *iii*) trade policy measures, insofar as they do not prohibit the entry or exit of goods into or from the customs territory of the Union.

#### Internal transit

Under the internal transit procedure, union goods may be moved from one point to another within the customs territory of the Union and pass through a country or territory outside the customs territory without undergoing any change in their customs status.

#### Storage

Under the storage procedure, non-Union goods may be stored in the customs territory of the Union without being subject to any of the following: *i*) import duties, *ii*) other charges provided for by other relevant provisions in force, or *iii*) trade policy measures, insofar as they do not prohibit the entry or exit of goods into or from the customs territory of the Union.

Union goods may be placed under the customs warehousing or free zone procedure in accordance with Union legislation governing specific fields, or in order to benefit from a decision granting the repayment or remission of import duties.

#### Specific use

#### Temporary admission

Under the temporary admission procedure, non-Union goods intended for re-export may be subject to specific use in the customs territory of the Union, with total or partial relief from import duties, and without being subject to any of the following: *i*) other charges provided for by other relevant provisions in force, or *ii*) trade policy measures, insofar as they do not prohibit the entry or exit of goods into or from the customs territory of the Union.

End-use

Under the end-use procedure, goods may be released for free movement under a duty exemption or at a reduced duty rate on account of their specific use.

#### Processing

#### Inward processing

Under the inward processing procedure, non-Union goods may be used in the customs territory of the Union in one or more processing operations without being subject to any of the following: *il* import duties, *il*) other charges provided for by other relevant provisions in force, or *ill*) trade policy measures, insofar as they do not prohibit the entry or exit of goods into or from the customs territory of the Union. The inward processing procedure may be used in cases other than repair and destruction only where, without prejudice to the use of production accessories, the goods subject to the procedure can be identified in the processed products.

#### Outward processing

Under the outward processing procedure, Union goods may be temporarily exported from the customs territory of the Union to undergo processing operations. The resulting processed products may be released for free movement with total or partial relief from import duties upon application by the holder of the authorisation or any other person established in the customs territory of the Union, provided that this person has obtained the consent of the holder of the authorisation and the conditions for the authorisation have been met

#### 10.2.2 Authorised Economic Operator (AEO)

An AEO is an economic operator, established in EU customs territory, that holds an AEO Certificate issued by the customs authorities of a Member State confirming that the operator meets all the parameters and conditions stated in articles 38 and 39 of the UCC and the Community Customs Implementing Provisions (Commission Delegated Regulation (EU) No. 2446/2015 and Commission Implementing Regulation (EU) No. 2447/2015).

All economic operators (manufacturers, importers, exporters, warehouse-keepers, operators authorised to carry out an activity in a free zone or in a free warehouse, transporters, forwarders, air freighters, terminalists, shipping companies, customs agents and, more generally, all operators whose activity involves the application of customs legislation) established in the EU can apply for an AEO Certificate.

The AEO Certificate gives an economic operator the Community status

of AEO for customs simplifications and/or security issues.

#### Advantages of the AEO Certificate

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- The AEO certificate allows the operator to enjoy a number of benefits, including:
  - being recognised on the market as a safe and reliable partner;
  - simplified procedures in obtaining customs simplifications;
  - more favourable treatment than other operators when it comes to physical and documentary customs inspections;
  - priority treatment of consignments if selected for inspection;
  - being able to choose the location of an inspection. The operator may opt for centralised customs clearance, provided for in article 179 of the UCC, which allows economic operators to centralise and supplement accounting, logistics and distribution functions, with consequent savings in administrative and transaction costs;
  - reduced data requirements for submitting summary declarations.
- Besides these "direct" advantages, having an AEO Certificate has the following "indirect" advantages:
  - · better relations with customs authorities (client coordinator);
  - · more timely shipments;
  - better security and communication between the parties in the supply chain;
  - customer loyalty;
  - · the prevention of problems since employees are known;
  - fewer safety-related accidents;
  - better planning;
  - fewer thefts and losses.

#### 10.2.3 BTI and BOI

It is worth highlighting some of the instruments of the European customs framework that can be used by European operators to provide one another with customs classification and origin certainty.

With regard to customs classification, the UCC provides for Binding Tariff Information (BTI), which is used to obtain the correct tariff classification for goods that operators intend to import or export.

Binding Origin Information (BOI) decisions, on the other hand, are decisions issued by European customs authorities related to the actual origin of the goods. Once issued, these decisions are binding on the authorities in all Member States in respect of goods imported or exported, provided that the goods and the circumstances determining the acquisition of origin are identical in every respect to what is described in the BOI.

Applications for binding information shall be made in writing either to the competent customs authorities of the Member State or Member States in which the information is to be used, or to the competent customs authorities of the Member State in which the applicant is established.

It is worth highlighting that under the UCC, the validity period of both BTI and BOI is three years, and that it is binding not only on the customs authorities, but on the applicant as well.

#### 10.2.4 Dual Use

Dual-use items are finished or semi-finished products, equipment and machinery components – including software and technology – that are normally used for civilian purposes but may have military applications, or may contribute to the proliferation of weapons of mass destruction.

Dual-use items are generally marketed for civilian purposes, but are also used to construct weapons.

Dual-use items are subject to specific rules that take account of the particular sector they belong to.

The EU therefore controls the export, transit and brokering of dual-use items that affect the research and development (R&D), production and trade of typically high-tech, advanced products across a wide-range of civil industries – e.g. energy, aerospace, defence and security, lasers and navigation, telecommunications, life sciences, chemical and pharmaceutical industries, material-processing equipment, electronics, semiconductor and computing industries, medical and automotive industries.

The export of dual-use goods and technologies is governed by a variety of standards, criteria and application procedures drawn up in accordance with national and international security requirements, such as:

Regulation (EC) No. 428/09, which establishes a general Community regime for the control of exports of the dual-use items and technology listed.



### 10.3 Excise duties

Excise duties are indirect taxes on the consumption of certain products:

- energy products;
- alcohol and alcoholic beverages;
- manufactured tobacco.

The authority responsible for the collection of excise duties in Italy is the *Agenzia delle Dogane*, the Italian Customs Authority.

#### Requirements and authorisation

Excise goods are subject to excise duties upon their production or import into the European Community.

Typically, excise duties are levied when goods are released for consumption. The goods are also considered as having been released for consumption:

- when stock shortages are higher than those provided for by law;
- the departure (including illegal departure) of goods from a suspensive arrangement;
- the manufacture or import (including illegal manufacture or import) of goods outside a suspensive arrangement.

For the circulation of excise goods, it is necessary to comply with certain formalities, including the lodging of specific documentation.

## 10.4 Import VAT

In the Community context, all imports are liable to VAT.

From an Italian perspective, VAT is owed when goods are introduced into Italy by the declarant. VAT must be paid by the owner of the goods or by the holder of the goods at the crossing of the customs border.

The following transactions are regarded as imports:

 the release of goods for free movement under a suspension of payment of customs duties, if the goods are destined for another Member State of the European Community;

- inward processing (temporary import). These operations are not regarded as imports for customs purposes, but are liable to VAT in Italy if the goods are introduced into Italy for sale or home use;
- the temporary admission of goods for re-export without processing; these goods do not benefit from total exemption from import duties in accordance with Community law;
- the clearance for home use of goods originating from Mount Athos, the Canary Islands, or French Overseas Departments;
- · re-imports for temporary export (outward processing);
- the re-introduction of goods previously exported.

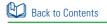
#### The tax base for VAT purposes and the release of goods

The tax base for VAT on imports is calculated in accordance with Italian VAT law and customs law.

## 10.5 Relations with the Italian customs authorities

In the past, the Italian customs authorities were known for being very conservative. Since the introduction of the AES framework in 2007, their approach has changed significantly. They have now modernised their procedures, also as a result of new Community legislation, which is binding on all Member States.

With this new approach, very interesting customs planning solutions are now possible, with the support of the authorities and a significant simplification of the global customs burden (formalities and duties).



## 11. Tax audits

## 11.1 Statute of limitations

Under ordinary rules, a tax year becomes time-barred for CIT and VAT purposes on 31 December of the fourth year following that in which the tax return for that year is filed. Starting with assessments on the 2016 tax year, a tax year will become time-barred on 31 December of the fifth year following that in which the tax return for that year is filed (e.g. for those taxpayers for whom the tax year follows the calendar year, the 2015 tax year, the tax return for which is filed in 2016, will become time-

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barred on 31 December 2020, but the 2016 tax year will become timebarred on 31 December 2022). If the tax return is not filed, the statute of limitations is extended by one year for assessments on tax years up to and including the 2015 tax year, and by two years for assessments on the 2016 tax year and beyond).

For assessments on tax years up to and including the 2015 tax year, if tax inspectors detect a violation that could constitute a criminal tax offence, and inform the public prosecutor before the ordinary statute of limitations indicated above expires, the term doubles for assessment purposes (e.g. the 2015 tax year becomes time-barred on 31 December 2024). Starting with assessments on the 2016 tax year, this extension will no longer apply (i.e. the 2016 tax year will become time-barred on 31 December 2022 even if tax inspectors detect a violation that could constitute a criminal tax offence).

For registration tax and other indirect taxes that apply equivalent rules (e.g. cadastral and mortgage tax), the authorities can assess additional taxes for up to two or three years (based on the type of violation claimed) from the date the deed (e.g. a contract) was filed for registration. If the deed such taxes apply to was not filed for registration, authorities can assess taxes due up to 5 years from the day the deed was supposed to be registered.

### 11.2 Post-audit actions

A tax audit usually ends with tax inspectors issuing an audit report (referred to as the PVC - *processo verbale di constatazione*). The tax audit report is not in itself an immediate source of liabilities. Major taxes, penalties and interest are applied upon authorities serving a formal notice of assessment before the statute of limitations expires. The tax authorities cannot serve the notice of assessment until 60 days have passed from the audit report being issued. This is to allow the taxpayer to file observations and comments on the audit, which the tax authorities should take into account when formulating the notice of assessment. The 60-day term does not apply to the taxpayer, who can file observations and comments before the notice of assessment is served.

After a tax audit ends, the taxpayer can seek a settlement or compromise with the authorities, or initiate, after the assessment deed has been served, litigation proceedings under one of the following procedures (this list is not exhaustive and merely represents those Back to Contents

procedures applied most commonly).

#### Pre-hearing compromise

Either before or after the notice of assessment is served, the taxpayer can request to negotiate with the tax authorities to see if there is room to reach a settlement. This is known as a "pre-hearing compromise" procedure. The pre-hearing compromise request is never binding (i.e. it does not oblige the parties to reach an agreement).

If a pre-hearing compromise is reached, penalties ordinarily applicable on the claimed violations are reduced to a third and are limited to those calculated on the amount of the adjustment agreed upon in compromise.

A pre-hearing compromise request submitted after the final notice of assessment has been served has the effect of extending the term to appeal (ordinarily 60 days) by an additional 90 days (to 150 days in total). If the taxpayer files a request for a pre-hearing compromise before the notice of assessment is served (and no settlement is reached), he cannot do so again after the notice of assessment has been served, and the 90 days extension is not granted.

#### Mediation

For all tax assessments issued by the Italian tax authorities of a value up to EUR 20,000, the taxpayer must launch advanced mediation proceedings. Mediation is compulsory, and if proceedings are not initiated, the appeal is barred from prosecution; if the mediation procedure is unsuccessful, the taxpayer may start litigation proceedings. If an agreement with the authorities is reached during the mediation procedure, penalties calculated on the agreed level of adjustment are reduced to 35 percent.

#### Appeals before the tax court

If the taxpayer is unable to reach an acceptable agreement under the pre-hearing compromise procedure and the authorities serve a notice of assessment, the natural subsequent course of action would be to file an appeal before the local tax court.

There are three levels of tax court in Italy: the local tax court, regional tax court, and supreme tax court.

The appeal must be filed within 60 days of the date on which the final notice of assessment is served. If a pre-hearing compromise is requested on paper (and was not requested before the final

assessment), an additional 90 days will be granted to file the local court appeal (see above).

The appeal does not suspend collection per se: the final notice of assessment becomes enforceable after 180 days, and the taxpayer must file for a provisional deposit. Under certain circumstances, the taxpayer can submit an application to the local court to have collection suspended.

If the taxpayer instead abandons litigation proceedings and accepts the notice of assessment without appeal by paying the amount claimed within 60 days, penalties are reduced to a third of the amount claimed.

#### Judicial conciliation (compromise after appeal)

After an appeal has been filed, the taxpayer (as well as the tax authorities) may still ask for partial or total judicial conciliation.

If conciliation, which requires the agreement of the parties, is reached, penalties calculated on the agreed level of adjustment are reduced to 40 percent where the agreement takes place before the local tax court hearing. Under recent changes to the law, if the agreement is reached after the hearing before the local tax court, penalties are reduced to 50 percent.

#### Voluntary disclosure

Under new procedures, after an audit has ended but before the notice of assessment is served, the taxpayer can correct mistakes according to the indications of the audit report by paying the tax corresponding to the findings of the authorities. In such an event, penalties are reduced to a fifth of the minimum applicable amount. If the voluntary disclosure is filed before the audit ends, penalties are discounted to a sixth.

## 11.3 International alternative dispute resolution procedures

In recent years, a large number of audits have focused on transfer pricing challenges. Within multinational groups, transfer pricing adjustments can cause double taxation. There are two instruments in place to remove double taxation: one consists of a mutual agreement procedure (MAP) filed under the European Arbitration Convention (typically activated when adjustments affect two or more European jurisdictions), the other is represented by a similar procedure submitted under the applicable double tax treaty (open to private individuals and non-European jurisdictions).

Procedures filed under the Arbitration Convention give certainty of double taxation removal as, where the competent authorities do not reach an agreement, a second arbitration phase begins, during which a decision on the final adjustment to apply is always made. This is not the case under double tax treaties, where, with the exception of the few conventions that contain arbitration clauses, the competent authorities must only endeavour to reach an agreement.

It is worth considering how an MAP under the Arbitration Convention interacts and conflicts with domestic litigation procedures before the tax court. Indeed, the competent Italian authorities take the view that when the local tax court delivers a decision, the authorities are not obliged to adhere to the outcomes of an MAP which is more favourable to the taxpayer. The taxpayer should therefore withdraw from the appeal before the tax court before the Arbitration Convention procedure ends.

Similarly, if, after the audit, a pre-hearing compromise is reached, the competent Italian authorities will not initiate any mutual agreement procedures.



# 12. How to invest in Italy

### 12.1 Types of transaction

#### 12.1.1 Share deals

In a share deal (i.e. the acquisition of shares in a target company), the capital gain realised by an Italian resident seller - calculated as the difference between the sale price and tax basis of the shares sold - may be partially exempt from tax, provided that the participation exemption requirements are met.

However, the buyer does not obtain tax recognition of the excess cost paid for the shares over the underlying net book value of the target. In other words, the tax values of the assets and liabilities of the target remain unchanged after the acquisition unless the buyer applies, if certain conditions are met, for the special regime allowing the step-up of the intangible goods, paying a 16 percent substitute tax, included in the participations acquired and accounted for in the consolidated financial statements.

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The sale of shares is not subject to VAT but is generally subject to a fixed registration tax of EUR 200.00.

The transfer of ownership of shares (in companies incorporated in Italy as S.p.a.s or S.a.p.a.s) is subject to a financial transaction tax (Tobin Tax) at a standard 0.2 percent rate, which is applied to the value of the transaction. The tax rate is reduced to 0.1 percent for transfers that take place on regulated markets and multilateral trading systems. No financial transaction tax applies to the transfer of ownership of quotas in companies incorporated as "società a responsabilità limitata".

The transaction value generally means the purchase price, the net balance of transactions concerning the same financial instrument and concluded on the same day by the same subject, the price contracted, or, failing that, the normal value determined according to consolidated income tax rules

There are certain exemptions from the financial transaction tax (i.e. shares transferred between related parties or share transfers related to restructuring operations as defined by article 4 of EU Directive No. 2008/7).

#### 12.1.2 Asset deals

An asset deal allows the buyer to acquire only the business segment actually needed, leaving the unwanted assets and liabilities behind. Consequently, an asset deal may be used where a target company has significant contingent tax liabilities, because it reduces the associated risk. Nevertheless, the buyer of a business unit (which qualifies as a going concern) is jointly liable with the seller for all tax liabilities and penalties incurred in the year of acquisition (up to the acquisition date) and the two previous years.

The liability of the buyer is, however, limited to the lower of (i) the value of the business unit acquired, and (ii) the tax liabilities of the seller already assessed by the tax authorities or under assessment in the year when the transaction takes effect and in the two previous years. It is possible to obtain a clearance certificate from the Italian tax authorities, attesting to the extent of the tax liabilities for which joint tax exposure exists. In this case, the buyer's liability is limited to the amounts indicated in the certificate. If the certificate is not issued within 40 days of application, or does not indicate any tax liability, the buyer is freed from any tax risk associated with the business unit acquired. No liability limit applies if the transaction involves tax fraud. Tax fraud is assumed to have been committed if the transaction is made within six months of a tax infringement resulting in criminal penalties.

In an asset deal, the tax basis of the asset acquired is equal to the purchase price of the business unit. The seller will realise a taxable

capital gain equal to the difference between the sale price and the tax basis of the business unit sold (the 24 percent, 27.5 percent up to 31 December 2016, IRES charged on the capital gain can be spread over a five-year period if the business unit has been held by the seller for more than three years).

Essentially, in an asset deal the seller is fully subject to tax on the capital gain realised while the buyer obtains tax recognition of the purchase price paid. Goodwill can be amortised for tax purposes over a minimum of 18 years (at an amortisation rate of 5.56 percent per year).

The disposal of a business unit is not subject to VAT, but it is subject to registration tax at different rates depending on the assets transferred (3 percent on goodwill, 0.5 percent on receivables, and 9 percent on real estate). Although registration tax should be split between the parties, it is often paid by the buyer under specific clauses in the sale and purchase agreement.

The fair market value of the transferred business unit is subject to assessment by the registration tax office. Therefore, it is advisable to obtain an appraisal from an independent expert beforehand, to be used as documentary evidence in the event of a tax assessment.

A common way of structuring an asset deal is to hive off the target business segment into a Newco in exchange for Newco shares, and then sell the shares in the Newco to the buyer. In this transaction:

- the contribution of the business segment to the Newco is neutral for tax purposes. In other words, any capital gain made on the contribution in the statutory accounts is ignored for tax purposes and the Newco will not obtain any step-up in the tax basis of the assets received;
- the tax basis and aging period of the business segment contributed to the Newco will be rolled over to the shares in the Newco;
- the subsequent sale of shares can be covered by the participation exemption, so that any capital gain is taxed at an effective rate of 1.2 percent (resulting from the application of the IRES tax rate, 24 percent, to a tax base of 5 percent of the capital gain amount, 1.375 percent up to 31 December 2016).

From a buyer's perspective, the Newco brings with it the option, as an alternative to the ordinary tax regime, of realigning the tax basis of the business segment to the statutory basis by paying a substitute tax on the step-up, at the following rates:

- 12 percent on the first EUR 5 million of the step-up;
- 14 percent on any amount between EUR 5 and EUR 10 million;
- 16 percent on any further amount.

The stepped-up assets are subject to ordinary amortisation/depreciation tax rules. The substitute tax is paid in three instalments over three years.

An alternative substitute tax regime grants the possibility of applying a 16 percent substitute tax on:

goodwill;

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- brands or trademarks;
- other intangibles (with an indefinite useful life).

The alternative substitute tax regime provides for accelerated amortisation. In this way, the cost of goodwill and brands can be amortised for tax purposes over five years (10 years for transactions completed up to the 2015 financial year) instead of 18, regardless of the amortisation charged to the statutory profit and loss account. The increased tax base cost is recognised from the second tax year following the transaction.

The contribution of a business segment is not subject to VAT. Registration tax of EUR 200.00 is due.

Asset deals and contributions of business segments are generally subject to anti-avoidance scrutiny. The Italian tax authorities may try to recast the contribution of a going concern followed by the disposal of Newco shares, ordinarily subject to EUR 200.00 registration tax, as a sale of going concern with ensuing proportional registration tax claim when the transaction lacks genuine business reasons.

#### 12.1.3 Mergers

The merger of two or more companies is tax-neutral and does not lead to the realisation or distribution of capital gains or losses. The tax neutrality of this transaction implies that:

- all the assets and liabilities of the absorbed companies are taken over by the surviving company on a tax-neutral basis, i.e. without any stepup in their tax basis;
- any merger difference (merger surplus/deficit) is disregarded for tax purposes (i.e. is not taxable/deductible);
- all the rights and obligations (including taxes) of the absorbed companies are transferred to the company resulting from the merger, starting from the date on which the merger takes effect.

The tax-deferred reserves of the merged companies are included in the taxable income of the company resulting from the merger, unless the reserves are reinstated in its balance sheet. However, reserves that are taxable only upon distribution are taxable if and to the extent that:

the merger surplus is distributed; or

 the increase in share capital exceeding the sum of the share capital of the companies participating in the merger is repaid to the shareholders.

While a merger is generally a tax-neutral event, the tax recognition of excess merger costs can be obtained under the substitute tax regime.

The remaining tax losses (and interest carry forwards) of the companies involved in the merger is subject to the following tests.

- Business vitality test: the profit and loss account of the company whose losses are to be carried forward must show, for the financial year prior to the merger resolution, revenues and labour costs higher than 40 percent of the average values of the two previous financial years.
- Net equity test: the tax loss carry forwards must be within the limit of the statutory net equity of the entity before the merger (disregarding any contributions obtained in the two years preceding the merger).

For tax losses, such limitations do not apply in the event of a merger between entities that are part of the same tax group.

Starting from 1 January 2017, it is also possible to carry forward any excess ACE tax benefit, subject to the business vitality test and net equity test.

The tax effects of the merger can be backdated to the beginning of the tax year in which the merger takes place. In this scenario, the business vitality and net equity test must also be applied to the tax losses, interest carry forwards and excess of ACE benefit accrued in the interim period.

A merger is not subject to VAT. In general, each merger is subject to a flat rate registration tax of EUR 200.00.

Mergers could be scrutinised for anti-avoidance.

#### 12.1.4 Demergers

As a general rule, demergers are tax-neutral. A demerged company can freely choose which assets and liabilities to contribute to the beneficiary.

The tax neutrality of this transaction implies that:

- Demerger differences (i.e. demerger deficits/surpluses) are disregarded for tax purposes (i.e. are not taxable/deductible). Therefore, demerged and beneficiary companies are not subject to corporate tax on any capital gains realised on the transferred assets.
- Starting from the effective date of the demerger, certain tax items

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(e.g. tax deferrals on capital gains realised in previous years, tax loss carry forwards) are transferred from the demerged company to the beneficiary in proportion to the net equity transferred. If, however, certain privileges and obligations (e.g. provisions for accelerated depreciation) are attached to particular assets or liabilities transferred to a specific company, they must be attributed to that company.

In order to preserve the tax neutrality of reserves subject to tax deferral and included in the net equity of the demerged company, the beneficiary company must create such reserves after the demerger, in proportion to the increase in its own net equity as a result of the transaction. Tax losses to be carried forward of the demerged company can be transferred to the beneficiary company in proportion to the net equity transferred to it, provided that – as in mergers – the business vitality test and net equity test are carried out.

Starting from January 1, 2017, it is also possible to carry forward any excess ACE tax benefit and interest carry forwards, subject to the business vitality test and net equity test.

While a demerger is generally a tax-neutral event, a step-up in the assets resulting from the merger can be obtained subject to certain conditions.

Demergers are not subject to VAT. A flat rate registration tax of EUR 200.00 is due.

Demergers could be scrutinised under anti-avoidance provisions. The Italian tax authorities may try to recast a demerger (especially when the assets transferred are real estate properties) followed by the disposal of the beneficiary company shares, ordinarily subject to EUR 200.00 in registration tax, as a sale of going concern with ensuing proportional registration tax claim when the transaction lacks genuine business reasons.

### 12.2 Listing a company in Italy overview

Companies registered in Italy may list their shares on one of the markets managed by Borsa Italiana. These markets can also be accessed by non-Italian companies through a primary listing, if the company is not yet listed, or a 'dual' or 'secondary' listing if the company is listed on its national or other stock market. In the case of the latter, specific regulations apply to the foreign company. EU directives on financial markets and the admission of financial instruments to public trading have been endorsed by the Italian parliament and are fully applicable in Italy, e.g. the Prospectus Directive, and the Markets in Financial Instruments Directive (MiFID).

The main markets available in Italy for the listing of shares are the following.

 Mercato Telematico Azionario – MTA: Borsa Italiana's main market (MTA) is mainly designed for medium-sized and large companies seeking to raise financial resources to fund a growth project. The MTA is a regulated market subject to stringent requirements in line with the expectations of professional and private investors. Within the MTA market, the STAR segment is dedicated to mid-capital companies that voluntarily comply with exceptional standards of liquidity, information transparency and corporate governance.

The MTA mainly supports companies in raising domestic and international financing from institutional and professional investors on one side and retail investors on the other side, and has always registered high liquidity performances. Companies are admitted to the MTA on the basis of both formal and substantive requirements.

Among the formal requirements are a market capitalisation at least EUR 40 million and a free float of at least of 25 percent (35 percent in the case of STAR companies). The substantive requirements include having a sound and clear strategy, a good competitive advantage, a balanced financial structure, managerial autonomy and all of the aspects that contribute to improving the company's ability to create value for investors.

The adoption of the *Codice di Autodisciplina* (Corporate Governance Code) is recommended to all companies listed on the MTA on a "comply or explain" basis. STAR companies are requested to comply with specific governance requirements. The companies listed on the MTA and the MIV are represented by the FTSE Italia index series, which is reviewed on a quarterly basis to ensure that companies are always included in the index that can most appropriately represent them.

MTA companies are included in indices according to their characteristics: the top 40 companies in terms of size and liquidity are included in the FTSE MIB index. STAR companies, in addition to being included in the indices pertaining to the MTA, also have their own specific index. Within the MTA market are two different segments.

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- The star segment: is the market segment dedicated to mid-size companies with a market capitalisation of less than EUR 1 billion, which voluntarily adhere to and comply with the following strict requirements:
  - high transparency and high disclosure requirements;
  - high liquidity (free float of a minimum of 35 percent);
  - corporate Governance in line with international standards.
- The international segment: is the new segment within Borsa Italiana's MTA regulated equity market dedicated to the trading of shares of non-Italian issuers already listed in other EU-regulated markets. The segment enables companies to trade some of the most liquid shares in the Euro area on the MTA fungibly within their primary market, whilst benefiting from Borsa Italiana's efficient and cost-competitive trading and post-trading infrastructure.
- AIM Italia: the Borsa Italiana market devoted to Italian small and medium-sized enterprises with high growth potential. The Market was born on 1 March 2012 from the merger of the AIM Italia and MAC market, to streamline the offer of markets devoted to SMEs and propose a single market for Italy's more dynamic and competitive SMEs, with a formula that leverages on the know-how obtained from more than 15 years of experience of the British AIM on one side and the specific needs of the Italian entrepreneurial system on the other. It is designed to offer a faster and more flexible procedure to listing whilst protecting investors at the same time, thanks to an efficient regulatory system that meets the needs of small businesses and specialised investors. Admission is not required to publish a prospectus under the Prospectus Directive, and is subsequently not required to publish quarterly management reports. Companies applying to AIM Italia must appoint a nominated adviser ("Nomad") from an approved register held by Borsa Italiana. The Nomad is responsible for guiding and advising the company on its responsibilities under AIM Italia rules during the admission process and on its continuing obligations in its subsequent life as a publicly quoted company.

AIM Italia offers companies a unique combination of advantages.

- AIM Italia enables smaller sized companies to access the market in a shorter space of time and at a lower cost than through the main market, ensuring transparency and liquidity for investors in the meantime.
- International visibility: AIM Italia gives companies access to a highly global market, benefiting from international visibility and enjoying

the credibility of the British AIM and the markets of Borsa Italiana.

- Shorter admission procedure: AIM Italia is designed to offer both a simplified listing process and post-listing formalities modelled on the structure of small and medium-sized companies.
- A Nomad (Nominated Adviser): the Nomad is the adviser who supports your company during the admission phase and throughout its time on the market, and is of central importance.
- Easier admission requirements than for the primary market: AIM Italia offers fewer admission criteria in terms of market capitalisation and floating (with a minimum rate of 10 percent).
- There are no particular corporate governance requirements and no specific economic and financial requirements.

The following table illustrates the main admission and ongoing requirements for the MTA and AIM Italia.

|                              | МТА  | AIM Italia                     |
|------------------------------|--|--------------------------------|
| Listing requirements         |  |                                |
| Free float                   | 25 percent                                 | 10 percent                     |
| Audited financial statements | 3  | 1 (if existing)                |
| GAAP                         | International                              | Italian or international / USA |
| Investors                    | Institutional / Retail                     | Institutional                  |
| Other documents              | Prospectus / MIS / Business Plan /<br>QMAT | Admission document             |
| Market cap (EUR)             | Min EUR 40 million                         | No formal requirements         |
| BOD (independent directors)  | Recommended (Corp. Gov. Code)              | No formal requirements         |
| Internal audit committee     | Recommended (Corp. Gov. Code)              | No formal requirements         |
| Remuneration committee       | Recommended (Corp. Gov. Code)              | No formal requirements         |
| Incentives to top management | Recommended (Corp. Gov. Code)              | No formal requirements         |

| Investor Relator           | Recommended  | Not mandatory   |
|----------------------------|--|---|
| Website                    | Mandatory  | Mandatory   |
| Main Advisor               | Sponsor / Global coordinator   | Nomad   |
| Key continuing obligations |  |   |
| Corporate Governance       | Comply or explain  | Optional  |
| Specialist                 | Optional (liquidity provider)  | Mandatory (liquidity provider)                        |
| Disclosure                 | Price sensitive information and M&A<br>(TUF and Consob Rules on Issuers) | Price sensitive and extraordinary operations required |
| Takeover code              |  | OPA Statutaria (Statutory OPA)                        |
| Related parties            | Procedures and reporting requirements                                    | Easy procedures and disclosure obligations            |
| Quarterly data             | I-III quarterly report within 45 days of the<br>quarter end              | NO  |
| Half year data             | Within 60 days of the half year end                                      | Yes – within 3 months of the half year end            |
| Annual report              | Within 120 days of the year end  | Yes – publication within 6 months of the year end     |



# Investment In Italy

Glossary

Definition

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Term

| ax return                 | The income tax return that must be completed by physical persons who are employees, pensioners, members of co-operatives and taxpayers with fixed-term contracts.  |
|---------------------------|--|
| Stability Law             | Law no. 190 of 23 December 2014  |
|                           | Allowance for Corporate Equity   |
|                           | Authorised Economic Operator<br>An economic operator established in EU customs territory that meets the requirements laid down by<br>the CCC and the CCIP.   |
|                           | Automated Export System<br>Ensures that exports started in one Member State can be concluded in another without the same<br>information having to be submitted.  |
| Italia                    | Borsa Italiana's market for small and medium-sized markets with high growth potential.   |
| yrafe                     | The Office of Records of the Resident Population in Italy  |
|                           | Advance Pricing Agreement<br>An arrangement with Italian tax authorties that determines, in advance of controlled transactions, an<br>appropriate set of criteria for the determination of the transfer pricing for those transactions (OECD<br>2010 Transfer Pricing Guidelines definition) |
|                           | Business-to-Business<br>A situation in which one business engages in a commercial transaction with another.  |
| 5                         | Base Erosion and Profit Shifting<br>Refers to tax planning strategies that exploit gaps and mismatches in tax rules to artificially shift<br>profits to low or no-tax locations, resulting in little or no overall corporate tax being paid. (OECD<br>definition)                            |
| k List                    | Refers, according to context, to the Black List for Cost Deduction or the CFC Black List.  |
| k List for Cost<br>Iction | For the purposes of applying the rules on the deduction of costs and expenses arising in foreign countries, the jurisdictions listed in the Ministerial Decree of 23 January 2002, as modified by the Ministerial Decree of 27 April 2015.   |
|                           | Binding Origin Information<br>Origin information that is binding on the administrations of all EU Member States when certain<br>conditions are met   |
| a Italiana                | Borsa Italiana S.p.A. – Italy's main stock exchange.   |
|                           | Binding Tariff Information<br>Tariff information that is binding on the administrations of all EU Member States when certain<br>conditions are met.  |
| tal Markets Union         | A union envisaged by the European Commission as a way of mobilising capital in Europe.   |
| usel fraud                | Also known as Missing Trader Intra-Community (MTIC) fraud, this involves the exploitation of the VAT-free movement of goods by criminal groups, who then sell the goods on, charging VAT that they never pay to the government.  |
|                           | <b>Community Customs Code</b> – Council Regulation (EEC) No. 2913/92 of 12 October 1992 establishing the Community Customs Code  |

| CCIP                                | <b>Community Customs Implementing Provisions</b> – Council Regulation (EEC) No. 2454 of 2<br>July 1993 laying down provisions for the implementation of Council Regulation (EEC) No. 2913/92<br>establishing the Community Customs Code   |
|-------------------------------------|---|
| CCNL                                | Contratto Collettivo Nazionale di Lavoro – National Collective Bargaining Agreement   |
| CFC                                 | <b>Controlled Foreign Company</b><br>A company which is resident or established in a low tax jurisdiction or anyhow benefits from<br>pereferential tax regimes as identified in a black-list and in which an Italian resident directly or<br>indirectly holds the majority of votes or exercises a dominant influence.  |
| CFC Black List                      | For the purposes of applying CFC rules, the jurisdictions listed in the Ministerial Decree of 21 November 2001, as amended by the Ministerial Decree of 30 March 2015.  |
| СІТ                                 | Corporate Income Tax: IRES and IRAP   |
| CONSOB                              | <b>Commissione Nazione per le Società e la Borsa</b> – National Commission for Companies and the Stock Exchange   |
| Convergence Regions                 | Italian regions with a GDP per capita of less than 75 percent of the average GDP of the EU-25, i.e. Campania, Apulia, Calabria and Sicily.  |
| Corporate Income Tax<br>Code        | Presidential Decree no. 917/1896  |
| Delega Fiscale                      | Law no. 23 of 11 March 2014<br>Provides for the principles to follow to simplify and streamline the Italian tax legislative framework.  |
| EBITDA                              | Earnings before interest, taxes, depreciation and amortisation  |
| EEA                                 | European Economic Area  |
| EFSI                                | European Fund for Strategic Investments   |
| EIB                                 | European Investment Bank  |
| EIF                                 | European Investment Fund  |
| ERDF                                | European Regional Development Fund  |
| ESF                                 | European Social Fund  |
| ETR                                 | Effective Tax Rate<br>The effective tax rate for individuals is the average rate at which their earned income is taxed.<br>The effective tax rate for a corporation is the average rate at which its pre-tax profits are taxed.<br>An individual's effective tax rate is calculated by dividing total tax expense by taxable income. For<br>corporations, the effective tax rate is computed by dividing total tax expenses by the firm's earnings<br>before taxes. The effective tax rate is the net rate a taxpayer pays if all forms of taxes are included<br>and divided by taxable income.<br>(Investopedia) |
| European Investment<br>Advisory Hub | A joint initiative between the European Commission and the European Investment Bank constituting<br>a single access point for advisory and technical assistance services to strengthen Europe's<br>investment and business environment.   |

| FCE Case                          | European Court of Justice case C-210/04 concerning the VAT treatment of transactions between a head office and its branch   |
|-----------------------------------|---|
| FIFO                              | First-in first-out (accounting method)  |
| FY                                | Financial Year  |
| GAAP                              | Generally Applied Accounting Principles   |
| GDP                               | Gross Domestic Product  |
| GGE                               | Gross Grant Equivalent<br>The amount of aid due before taxes.   |
| Halifax Case                      | European Court of Justice Case C-255/02 concerning the avoidance of VAT.  |
| IAS                               | International Accounting Standards<br>A series of accounting standards, known as the International Accounting Standards, were released<br>by the IASC between 1973 and 2000, and were ordered numerically. The series started with IAS<br>1, and concluded with the IAS 41, in December 2000. At the time when the IASB was established,<br>they agreed to adopt the set of standards that were issued by the IASC, i.e. the IAS 1 to 41, but that<br>any standards to be published after that would follow a series known as the International Financial<br>Reporting Standards (IFRS). When the IASB was established in 2001, it was agreed to adopt all<br>IAS standards, and name future standards as IFRS. One major implication worth noting is that any<br>principles within IFRS that may be contradictory will definitely supersede those of the IAS. Basically,<br>when contradictory standards are issued, older ones are usually disregarded. |
| IFRS                              | International Financial Reporting Standards – the new set of accounting standards in place since 2001, which replaced the IAS.  |
| ΙМU                               | Imposta municipale propria – Municipal Property Tax   |
| INAIL                             | Istituto Nazionale per l'Assicurazione contro gli Infortuni sul Lavoro – National Institute for Accidents at Work   |
| INPS                              | Istituto Nazionale della Previdenziale Sociale<br>National Institute of Social Security   |
| Interest & Royalties<br>Directive | Council Directive No. 2003/49/EC of 3 June 2003 which provides that interest and royalty payments shall be exempt from any taxes of an EU Member State, provided that the beneficial owner of the payment is a company or permanent establishment in another Member State.  |
| IP                                | Intellectual Property<br>i.e. intellectual works, patents, trademarks, designs, models, processes, secret formulas and<br>industrial, commercial or scientific knowledge.   |
| IRAP                              | Imposta regionale sulle attività produttive: a regional business tax  |
| IRES                              | Imposta sul reddito delle società: corporation tax  |
| IRPEF                             | Imposta sul reddito delle persone fisiche: personal income tax  |
| ISTAT                             | Istituto Nazionale di Statistica – Italian National Institute of Statistics   |



| Italian Digital Agenda              | This comprises the body of initiatives and measures taken by Italy to implement the Digital Agenda for Europe  |
|-------------------------------------|--|
| пс                                  | Income Tax Code (TUIR – Testo Unico Imposte sui Redditi)   |
| IVAFE                               | Imposta sul valore delle attività finanziarie detenute all'estero – tax on the value of financial assets held abroad.  |
| IVIE                                | Imposta sul valore degli immobili situati all'estero – tax on the value of real estate held abroad   |
| Jobs Act                            | Comprised of Law Decree no. 34 of 20 March 2014 and Law no. 183 of 10 December 2014, this aims to reform the Italian labour market and make it more competitive.   |
| Juncker Plan                        | The European Commission's Investment Plan for Europe announced by European Commission<br>President Jean-Claude Juncker in November 2014.   |
| LIFO                                | Last-in last-out (accounting method)   |
| M&A                                 | Merger & Acquisition   |
| ΜΤΑ                                 | Mercato Telematico Azionario<br>Borsa Italiana's main market, mainly for medium-sized and large companies looking to raise funds for<br>growth.  |
| NPB                                 | National Promotional Bank<br>A legal entity carrying out financial activities on a professional basis which is given a mandate by<br>a State or State entity at central, regional or local level to carry out development or promotional<br>activities.                |
| Nulla Osta                          | Certificate of no impediment   |
| OECD Model Tax<br>Convention        | An agreement between the members of the OECD (Organisation for Economic Cooperation and Development) that lays down guidelines for negotiation of Conventions to avoid double taxation on income.  |
| OECD Transfer Pricing<br>Guidelines | These provide guidance on the application of the 'arms length principle'.  |
| ОЕМ                                 | <b>Original Equipment Manufacturer</b><br>A company that makes a part which is used in another company's product   |
| OIC                                 | Organismo Italiano di Contabilità – Italian Accounting Body  |
| P&L                                 | Profit and Loss  |
| Parent-Subsidiary<br>Directive      | Council Directive 90/435/EEC of 23 July 1990, as amended by Council Directive 2003/123/EC of 22<br>December 2003.<br>This provides for exemption from taxation in a Member State on dividends paid to qualifying Parent<br>Companies resident in another Member State. |
| Participation Exemption             | The exemption from taxation on qualifying dividends and capital gains realised on disposal of shares<br>or quotas, equivalent financial instruments and equity shares in partnerships.   |
| Patent Box                          | A regime under which a certain percentage of income deriving from the licensing or direct use of eligible IP is excluded from the tax base.  |

| Quota/quotas            | An equity interest in an Italian S.r.I. company.  |
|-------------------------|---|
| R&D                     | Research & Development  |
| REIF                    | Real Estate Investment Fund   |
| RW                      | The form Italian tax residents must use to declare all assets (income-producing assets and assets capable of generating future income or gains) held outside Italy.   |
| Schengen Agreement      | The treaty that led to the creation of the borderless Schengen Area in Europe, signed in 1985.  |
| Skandia Case            | European Court of Justice Case C-7/13 concerning the VAT treatment of transactions between a head office and its branch when a legal entity is part of a VAT group.   |
| SMEs                    | Small and Medium-Sized Enterprises  |
| SPV                     | Special Purpose Vehicle<br>A legal entity created for a specific purpose.   |
| Taxpayers' Charter      | Law no. 212/2000 ("Statuto del contribuente")   |
| TFR                     | Trattamento di Fine Rapporto – severance pay  |
| ТОВ                     | Takeover Bid  |
| UCC                     | <b>Union Customs Code</b> – Regulation (EU) No. 952/2013 of the European Parliament and of the Council of 9 October 2013 laying down the Union Customs Code.  |
| Unico tax return        | The income tax return that must be completed by physical person and self-employed persons and professionalswith VAT numbers.  |
| VAT Directive           | Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax   |
| White List (white-list) | Published in the Ministerial Decree of 4 September 1996. Countries on the White List are jurisdictions that have an acceptable level of taxation and an exchange of information agreement with Italy. The list currently includes Albania, Algeria, Argentina, Australia, Austria, Bangladesh, Belarus, Belgium, Brazil, Bulgaria, Canada, China, Croatia, Cyprus, the Czech Republic, Denmark, Ecuador, Egypt, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, India, Indonesia, Ireland, Israel, Ivory Coast, Japan, Kazakhstan, Kuwait, Latvia, Lithuania, Luxembourg, Macedonia, Malta, Mauritius, Mexico, Morocco, Montenegro, the Netherlands, New Zealand, Norway, Pakistan, the Philippines, Poland, Portugal, Qatar, the Republic of Korea, Romania, Russia, San Marino, Serbia, Singapore, the Slovak Republic, Slovenia, South Africa, Spain, Sri Lanka, Sweden, Tanzania, Thailand, Trinidad and Tobago, Tunisia, Turkey, Ukraine, the United Arab Emirates, the United Kingdom, the United States, Venezuela, Vietnam and Zambia. |
| WHT                     | Withholding tax   |
| YoY                     | Year on Year  |

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