



Investment in Italy

2018

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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 2018. 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 implementing it, any advice obtained which is critical to the strategy should be confirmed.

KPMG in Italy

December 2018

Ninth Edition



Attracting foreign investment is a strategic priority of Italy's national economy

Despite its volatile markets and political instability, Italy is still the ninth biggest economy in the world and the third in the euro zone, after Germany and France, with a population of around 61 million and per capita GDP of around US\$27,000.

The country's main resource is household wealth because Italian families are big savers and have some of the lowest debt in Europe; this translates into potentially large spending and investment capacity.

Geographically, Italy is in a strategic location for international commerce: it is the crossroad of the European market, the bridge between Northern and Southern Europe, but also the port of departure to North Africa and the Middle East. The country has a very wide transport network, extending over some 180,000km and including 7,000km of motorways and more than

1,000km of high-speed rail track, as well as 300 ports, strategically distributed for Mediterranean trade over more than 7,000km of coast, and 130 airports.

For over 30 years Italy has been Europe's second biggest manufacturer, after Germany, and seventh worldwide.

To invest in Italy is to gain access to the very best know-how and skills in the machinery and automation, fashion and design, and food and wine industries. Recently, Italy has also opened its doors to foreign investment in sectors such as energy, distribution networks, telecommunications and transport.

Drivers of the Italian economy are the country's SMEs – leaders in global value chains and suppliers of high-quality semi-finished products.

Tertiary education is of a high standard and 15 Italian universities are listed among the world's top 500.



Research and innovation are tightly woven into industrial processes. Italy is one of the countries with the highest number of applications for the international registration of industrial designs, and third in the league table of countries with the highest number of trade mark applications in the agricultural and food industry. In the Global Innovation Index 2018, Italy's economy and enterprises rank 31st for innovation.

The artistic heritage of Italian cities is unrivalled.

The country has more world heritage sites than any other country on the UNESCO list. Each year some 50 million tourists head to Italy, making our country the fifth most popular tourist destination in the world.

In 2018, Italy rose from 43rd to 31st position in the World Economic Forum's Global Competitiveness Index.

Foreign investment is key to a country's growth: in Italy especially, investment can provide the capital that small businesses need in order to invest in innovation and skilled management and to retain their competitive edge in international markets. Attracting foreign investment is one of the strategic priorities of Italy's public authorities, which are developing policies to create an investor-friendly environment.

It is in this context that Investment in Italy sets out to be a practical guide to investors by giving a snapshot of the general economy, listing the incentives available, outlining the legal framework for special transactions, describing the basic bookkeeping and tax rules, and making useful suggestions on how to invest in Italy.

Domenico Busetto

International Tax Partner
KPMG in Italy, Tax & Legal



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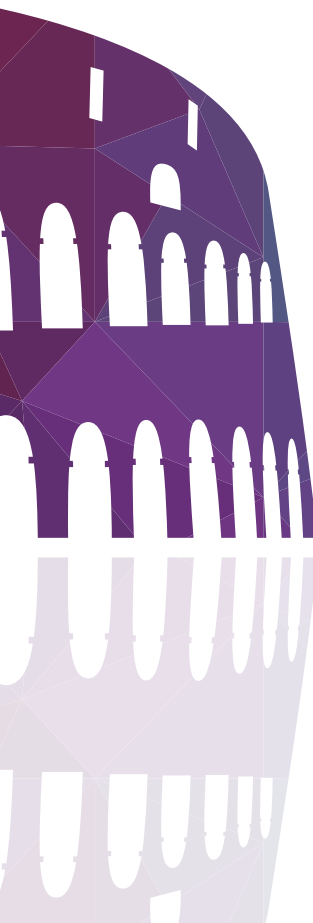
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1. Country overview



Italy, with a population of nearly 61 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 107 provinces, 14 metropolitan cities and approximately 8,000 municipalities. In 2018, 19 new municipalities were created through mergers, while 42 were abolished.

Rome, located in the Lazio region, is the largest Italian city (with nearly 2.9 million inhabitants). Milan in Lombardy (1.4 million inhabitants), Naples in Campania (1 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 23 percent, while the remaining 13 percent of the population falls within the 0-14 age group.





1.1 Transportation network

Airports



Railways



Italy has approximately 130 airports, handling about 175 million passengers and 1.1 million tonnes of freight per year.

One of its biggest international airports, Leonardo Da Vinci near Rome, handles about 41 million passengers per year.

More than 800 million passengers and over 90 million tonnes of freight travel by rail each year.

Italy has one of the safest railway networks in Europe and boasts 16,781km of track. The country has the fourth largest network in Europe after those of Germany, France and Ukraine.

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





Ports



There are approximately 30 major ports, handling 51 million passengers and 498 million tonnes of freight per year.

There are another 321 ports distributed along approximately 7,400km of coastline.

Roads



The national road network extends over approximately 180,000km.

The national motorway network extends over nearly 7,000km and makes up approximately 10 percent of the European motorway network.





1.2 Snapshot of the Italian economy

1.2.1 Main macro-economic indicators for Italy: 2012-2019

	2012	2013	2014	2015	2016	2017	2018	2019 (forecast)
Real GDP (EUR billion)	1,568	1,541	1,544	1,556	1,576	1,602	1,615	1,617
GDP (YoY changes)	-2.9%	-1.7%	0.2%	0.8%	1.3%	1.6%	0.8%	0.1%
Unemployment rate (% labour force)	10.7%	12.1%	12.6%	11.9%	11.7%	11.3%	10.6%	10.7%
Average nominal wage inflation	2.3%	2.1%	2.5%	2.5%	0.4%	0.6%	0.8%	0.7%
Consumer price index	3.3%	1.2%	0.2%	0.1%	0.0%	1.3%	1.2%	0.9%
Exports of goods and services (% change)	2.0%	0.9%	2.4%	4.2%	2.3%	6.3%	1.0%	0.6%
Imports of goods and services (% change)	-8.2%	-2.3%	3.1%	6.6%	3.9%	5.6%	2.0%	1.7%

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 SMEs and only 200,000 of the firms have over 10 employees. There are 3,800 large companies with more than 250 employees. While it is common for many European economies to have a vast majority of SMEs, a defining feature of Italian industry is the 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 is 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 sector. Tourism, retail and financial services represent a significant part of the sector.

The industrial sector accounts for 19.4 percent of GDP, with the remainder contributed by agriculture (source: ISTAT, 2017). 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 39.2 billion in 2017 (+7.7 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 2017, Rome was the main tourist destination in Italy with nearly 27 million stays (6.4 percent), followed by Milan with 12 million (2.8 percent), Venice with 11.6 million (2.8 percent), Florence with 10.1 million (2.4 percent), and Rimini with 7.4 million (1.8 percent).

Automotive

In 2018 the national market decreased by 3 percent on 2017, with more than 1.9 million passenger cars sold/registered. Approximately 26 percent of passenger car sales were made by FCA, while the highest-selling premium brand was Audi (Volkswagen Group). The three best-selling models in Italy in 2018 were the FIAT Panda, Renault Clio, and FIAT 500X.

The outlook is negative: registrations in 2019 will decrease slightly to 1,900,000 and rise slightly in 2020.

The fuel in most demand remains diesel: 51.2 percent of the cars registered in 2018 were diesel (56.5 percent in 2017). Alternative fuels are growing: in 2018, 124,565 dual-fuel petrol/LPG vehicles were sold (6.5 percent of the market, the same as in 2017), 86,626 hybrids (4.5 percent of sales, up from 3.4 percent in 2017) and 4,997 electric (up from 2,002 in 2017). Additionally, registrations of CNG cars returned to growth (37,406 against 32,751 in 2017).

Fashion and luxury

With revenues of approximately EUR 87 billion in 2017, up 2.8 percent on 2016, Italy has the most active fashion and luxury industries in the world and, without a doubt, this is one of the most 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 more than EUR 30 billion and Italy is the largest pharmaceutical manufacturer in the EU. Seventy-nine percent of the pharmaceuticals production is exported (EUR 24 billion). Sixty percent of pharmaceutical companies in Italy are foreign-owned (e.g. GlaxoSmithKline, Novartis, and Baxter) while the remaining 40 percent are Italian-owned (e.g. Recordati, Zambon, Angelini, Bracco, and Sigma-Tau). In 2017, investments in this sector totalled EUR 2.8 billion, and its workforce numbered 65,400 employees, 90 percent of whom were graduates.

The strong performance of exports in this sector is the result of the increased quality of the medicines and vaccines being exported all over the world: between 2007 and 2017 the average value of exports grew by 107 percent (compared to 74 percent across the EU).

Information and communication technology (ICT)

After years of decline, the Italian ICT market grew by 2.3 percent to EUR 68.7 billion in 2017, which was better than the previous year (+2 percent). The market in 2017 was driven by cloud (+21.5 percent), IoT (+17.4 percent) and mobile services (+11.9 percent). Telecom services as a whole decreased by 2.6 percent in 2017. Other positive sectors included digital content and advertising, up 8.0 percent, and software and ICT solutions, up 7.9 percent.

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 more than 10 percent. It is characterised by the stable presence of many leading foreign companies. The quality of Italian research and Italy's 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 Radici Group and Bracco Group) account for 27 percent of production, multinationals (e.g. BASF, Bayer, Air Liquide, and Linde) for 38 percent, and SMEs for 35 percent.





Aerospace and defence

With more than 45,000 employees (an estimated 160,000 in the entire production chain), in 2016 aerospace companies produced total revenues of EUR 13.5 billion (9.4 billion export value). The sector is characterized by high work-force productivity, high capital intensity, long investment cycles and high levels of R&D spending. Italy's expenditure on R&D in aerospace and defence, which accounts for 21.9 percent of its total R&D expenditure, is above the OECD average expenditure of 18.2 percent in this field. Italy is a leader in this sector, ranking among the first ten countries for production and fifth in the world for cumulative value of defence exports during the period 2007-2016, behind the USA, the United Kingdom, Russia and France.

Italy is home to several multinational companies such as Leonardo, Fincantieri, GE Avio, Iveco and Piaggio Aerospace. Eighty percent of the national production chain is formed by SMEs, mainly located in Piedmont, Lombardy, Lazio, Campania and Puglia.

Renewable energy

Italy is one of the most virtuous of the EU Member States in terms of renewable energy policies and measures: by 2013 it had already exceeded the 2020 energy savings target of 158 million tonnes, and 17.5 percent of its gross final consumption of energy is already from renewable sources (the target was 17 percent by 2020). Furthermore, Italy has the fifth biggest total installed wind-energy capacity in Europe (approximately 9.5 GW and approximately 6 percent of Europe installed capacity). National energy production from renewable sources reached 108 TWh (37.3 percent) in 2016 thanks to the 742,000 plants operating in Italy with 52.3 GW installed power. Hydroelectricity is still the most widely-used renewable source, accounting for 39 percent of electricity generation from renewables.

These figures are significant, as 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, which are a strategic feature of the Italian industrial system and, for some industries, 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 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.

Industrial clusters



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





1.2.4 Typical issues facing Italian medium-sized companies

Broad variety of legal forms

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

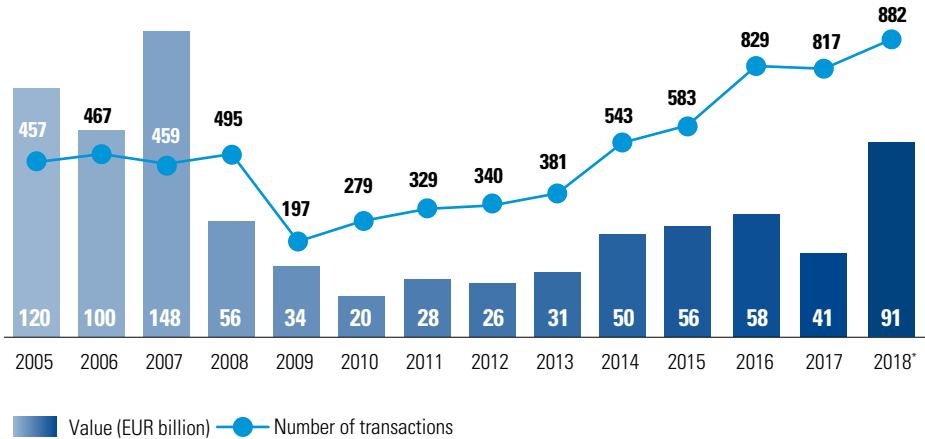
Employees are generally highly knowledgeable, experienced and skilled as a result of the Italian system of in-house apprenticeships and vocational studies. Employee remuneration is commonly subject to collective bargaining agreements enforced by strong trade unions. A potential investor should be fully 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 2005 to 2018: value and number of transactions



*Figure as at 15 December 2018

Source: KPMG Corporate Finance

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

After a period of public investment, mainly through the 'Cassa Depositi e Prestiti'¹, 2014 was a year of corporate reorganisations involving several leading Italian groups.

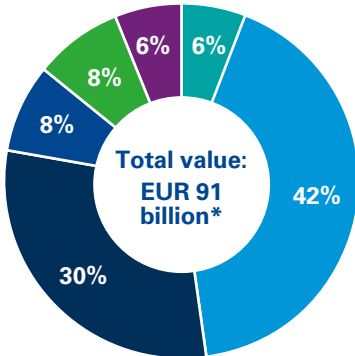
In 2018, the number of transactions (882) and their value (EUR 91 billion) increased.

- Italian-managed transactions abroad rose to 166, with a value of EUR 57 billion (in 2017 there were 159 transactions, with a value of EUR 9 billion).
- Foreign M&A operations in Italy increased to 276, with a value of EUR 18.4 billion, representing around one-third of the total (in 2017 there were 266 foreign-managed transactions in Italy).

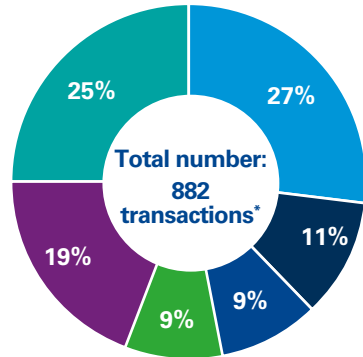
¹ Cassa Depositi e Prestiti is a joint-stock company, 82.8 percent owned by the Italian Ministry of Economy and Finance and 15.9 owned by various banking foundations. The remaining 1.3 percent is represented by treasury shares.



2018 M&A values by industry (target company)



2018 M&A number of transactions by industry (target company)



- Consumer Markets
- Energy & Utilities
- Financial Services
- Industrial Markets
- Support Services & Infrastructure
- Technology, Media & Telecommunications

(*) Figure as at 15 December 2018

Source: KPMG Corporate Finance







2. Incentives for investors

2.1 Main funding and facilities offered by Europe

2.1.1 Juncker Plan

The original investment plan for Europe (also known as the 'Juncker Plan'²) aimed to mobilise at least EUR 315 billion in private and public investment over three years (2015-2018). The so-called 'EFSI 2.0', described in more detail below, extends the lifetime of the fund and increases its investment target. The Juncker Plan goals are to:

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

The original investment plan for Europe had three parts, with a view to:

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

2.1.2 European Fund for Strategic Investments (EFSI and EFSI 2.0)

EFSI 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.

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 EFSI 2.0 regulation³ extends the lifetime of EFSI from mid-2018 to the end of 2020 and increases:

- its investment target from EUR 315 billion to at least EUR 500 billion (the fund is expected to achieve an overall multiplier effect of 1:15 and thus generate up to EUR 500 billion in investments in total);
- the EU budget guarantee to EUR 26 billion (EUR 16 billion of which was available for guarantee calls until mid-2018);
- the EIB's contribution to EUR 7.5 billion (from the current EUR 5 billion).

² *The European Commission's Investment Plan for Europe announced by European Commission President Jean-Claude Juncker in November 2014.*

³ *In December 2017, the European Parliament and Member States agreed on the EFSI 2.0 regulation, which became law on 30 December 2017.*





The main amendments contained in the EFSI 2.0 regulation and designed to improve the original EFSI are summarised below.

Increased transparency: under the new EFSI, the Investment Committee will publish its decisions online, explaining why it chooses a project to receive support from the EU budget guarantee. The scoreboard of indicators will be published after the signature of each EFSI project. The new regulation also gives a more detailed definition of what makes a project eligible for EFSI support, so-called 'additionality'.

Larger proportion of sustainable projects: at least 40 percent of EFSI infrastructure and innovation projects will aim to contribute to climate action in line with the Paris Agreement. EFSI 2.0 also explicitly targets new sectors: sustainable agriculture, forestry, fisheries and aquaculture, and other parts of the bio-economy.

Greater focus on small projects: given the success of EFSI in supporting small companies, the extended EFSI will increase the proportion of the guarantee for SMEs from 26 percent to 40 percent. The new EFSI also encourages the EIB group to help national promotional banks set up investment platforms to bundle several small-sized projects by theme or by region in order to attract investors.

More technical support at the local level: the European investment advisory hub, which is jointly managed by the Commission and the EIB, is proving a useful resource for businesses in need of technical support to get their projects off the ground. In EFSI 2.0, the work of the hub will be enhanced by providing more tailor-made assistance on the ground and working in close cooperation with national promotional banks.

Other improvements aim to ensure that the fund's support covers as many EU countries as possible.

2.1.3 Ensuring that investment finance reaches the real economy

A European investment project portal and a European investment advisory hub 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.

2.1.4 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 Union⁴ to reduce fragmentation in the financial markets and increase the supply of capital to businesses and investment projects.

2.1.5 Results and examples of EU funding used by Italy

In its first two and a half years, EFSI stimulated EUR 371.2 billion in new investments in 28 Member States and now aims to trigger EUR 500 billion by 2020. Some 856,000 SMEs and mid-cap companies are expected to benefit, gaining better access to finance.

⁴ A union envisaged by the European Commission as a way of mobilising capital in Europe.





Juncker Plan results in Italy by December 2018

Total financing under EFSI in Italy amounts to EUR 9.5 billion and is set to trigger EUR 55.2 billion in additional investments.

Infrastructure and innovation projects

- Eighty approved projects financed by the EIB with EFSI backing.
- Approximately EUR 7.0 billion in total financing.
- Set to trigger EUR 30.6 billion in total investment.

Small and medium-sized enterprises

- Seventy approved agreements with intermediary banks or funds financed by the EIF with EFSI backing.
- EUR 2.5 billion in total financing.
- Set to trigger approximately EUR 24.5 billion in investments with some 215,380 SMEs and mid-cap companies expected to benefit from improved access to finance.

Examples of EFSI-backed projects in Italy

Dolomiti Energia

- EFSI-backed financing: EUR 100 million.
- Set to trigger total investment: EUR 180 million.

The EIB is lending Dolomiti Energia EUR 100 million to renew and develop its gas and electricity distribution networks. The financing will strengthen and maintain hydroelectric plants in the province of Trento in northern Italy, the main area in which Dolomiti Energia operates and where it employs 1,400 people.

Telecom Italia: high-speed broadband

- EFSI-backed financing: EUR 500 million.
- Set to trigger total investment: EUR 1,808 million.

The EIB is providing EUR 500 million to Telecom Italia for the rollout of a new broadband access network (combined fibre and copper solutions) for ultra-high-speed broadband services in Italy. As a result of this financing, seven million more households will benefit from high-speed broadband, increasing the population coverage by 32 percent to 60 percent of all Italian households.

Echolight

Echolight is a medical technology company developing innovative ways to detect and diagnose osteoporosis at an early stage, through radiation-free echographic examination. It also offers a monitoring solution for osteoporosis that is easily accessible, so reduces waiting times at medical appointments. In 2016 the company received financing from Panakés, a venture capital fund that specialises in medical companies. The financing is guaranteed by the EIF under the Juncker Plan and has allowed the company to hire a number of scientists to carry out clinical studies in 15 different hospitals across Europe.

Umbria Legno: wooden furniture

Umbria Legno is a young company specialising in designing and manufacturing wooden garden furniture. Being a start-up with no credit history, Umbria Legno struggled to access financing to grow its business. The solution came through a bank loan with the help of Confidicoop Marche, backed by the Juncker Plan. The business is now growing and taking on new staff.





2.2 Main incentives offered by the Italian government

2.2.1 Development contracts

Development contracts (*contratti di sviluppo*) provide incentives for major investments in industry (including in businesses that process and sell agricultural products), tourism, environmental protection, 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 48 months of the date of approval of the application 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, also on behalf of any 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 (also in combination):

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

The size of the grant 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 environmental projects.

2.2.2 National Industry 4.0 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 IoT).

Italy has developed a National Industry 4.0 Plan, which includes various practical measures. The Ministry of Economic Development's main aims are to:

- promote all forms of advanced technology equally and impartially;
- 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 decision-maker.

The plan follows four strategic lines:

- **Innovative investments:** the aim is to stimulate private investments in Industry 4.0 technology drivers and increase private expenditure in R&D and innovation.
- **Enabling infrastructure:** the strategy is to ensure adequate network infrastructure and the security and protection of data, and to cooperate in establishing the IoT, open standards and interoperability criteria.
- **Expertise and research:** the focus is on developing skills and stimulating research through *ad hoc* training courses.





- **Awareness and governance:** the aim is to generate interest in Industry 4.0 opportunities and create shared public/private governance policies.

2.2.3 National Operational Programme for Research and Innovation

This programme offers EU funding to certain regions of Italy under the 'Investment for growth and jobs goal'. It 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 1,286 million.

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, agri-food, 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 educational 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 in skills and lifelong learning by developing educational and training infrastructure (22 percent);
- providing technical assistance to support the implementation of the programme (4 percent).

2.2.4 Invitalia

Invitalia is a 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. 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 Sanpaolo).

Invitalia supports international action plans to promote investment opportunities in priority sectors, assisting companies in developing business solutions and strategic partnerships. It also 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 agri-food 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 Regional investments

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 EU by 2020.

All Italian regions have issued 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.

In 2014-2020, Italy will manage around 50 operational programmes under the EU cohesion policy. For that period Italy has been allocated around EUR 32.2 billion (current prices) in total cohesion policy funding:

- EUR 22.2 billion for less developed regions (Campania, Puglia, Basilicata, Calabria and Sicily)
- EUR 1.3 billion for transition regions (Sardinia, Abruzzo and Molise)
- EUR 7.6 billion for more developed regions (Valle d'Aosta, Piedmont, Lombardy, Liguria, Veneto, the Province of Bolzano, the Province of Trento, Friuli Venezia-Giulia, Emilia Romagna, Tuscany, the Marches, Umbria, and Lazio)
- EUR 1.1 billion for European Territorial Cooperation

- EUR 567.5 million for the Youth Employment Initiative.

Regional programmes are also implemented for the specific purpose of benefitting from the ERDF and the ESP, described below.

2.3.1 European Regional Development Fund (ERDF)

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

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 Italian Digital Agenda⁵
- support for SMEs
- the low-carbon economy.

The amount of ERDF resources allocated to these priority areas 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 to 60 percent.
- In less developed regions (GDP per capita <75 percent of the EU-27 average), this drops further, to 50 percent.

⁵ The body of initiatives and measures taken by Italy to implement the Digital Agenda for Europe.





Moreover, 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 listed 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 geographical disadvantage (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 European Social Fund (ESF)

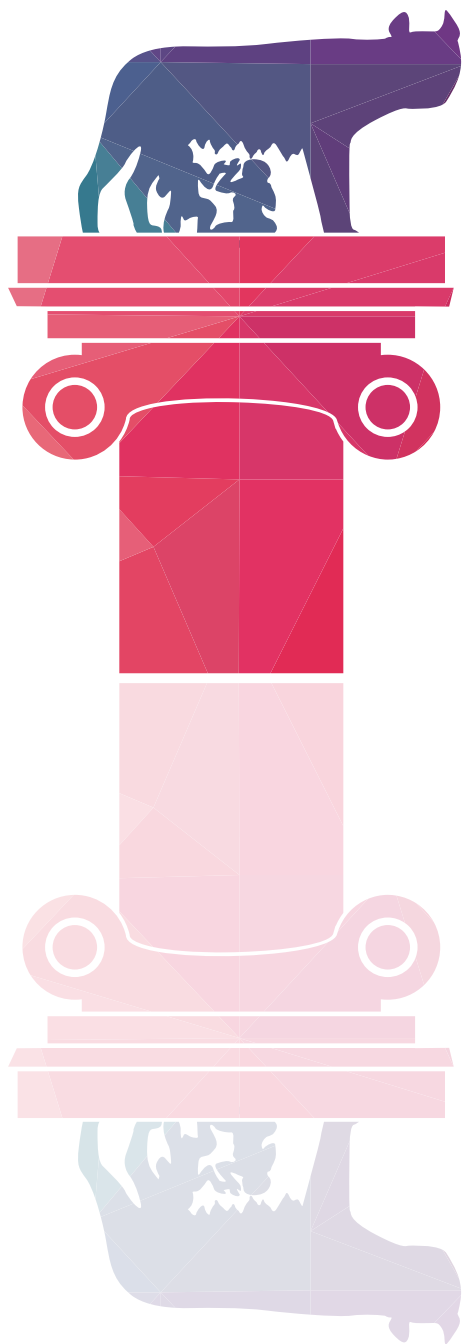
The ESF is Europe's main instrument for supporting jobs, helping people get better jobs, and ensuring fairer job opportunities for all EU citizens. It works by investing in Europe's human capital: its workers, young people and job hunters. ESF financing of EUR 10 billion a year is improving job prospects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

The EU 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 serious 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

There are no limits on investments made in Italy by nationals of other European Union Member States and such investments are treated in the same way as those made by Italian nationals.

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

Authorisations, and compliance with other conditions, may be necessary for investments in certain industries and regulated sectors (e.g. telecommunications and banking/financial intermediation) through the incorporation or 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, the extent of liability, and the tax and accounting implications.

There are two main categories of legal entities:

- (i) partnerships (*società di persone*)
- (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;
- (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 accomandanti*) have unlimited liability.

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: joint-stock 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

Upon formation, a joint-stock company requires minimum share capital of EUR 50,000, of which at least 25 percent (amounting to EUR 12,500) must be paid to the directors.

For companies operating in specific fields, such as insurance or banking, 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 formation of the company. There is no maximum number of shareholders. Shareholders of an S.p.A. can be either natural or legal persons and Italian or foreign (see above).

The capital is divided into freely transferable (the company's articles of association may set limits 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;
- (ii) a governing 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 by 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), management and control lies with a board of directors and a management control committee appointed from 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 that, in the traditional model, are the sole responsibility of 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 (this is lower for a simplified S.r.l. – see below) and at least 25 percent of it (EUR 2,500) must be paid to the directors.

The minimum capital of EUR 10,000 may also be built up over time ('progressive corporate capital') provided 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 formation 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.l.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.l.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.

Except in specific cases provided for by law, a limited liability company is not required 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 has 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 require the company to appoint a registered auditor or an audit firm.

Simplified S.r.l.s

In addition to the ordinary model, there is another type of S.r.l. – a simplified limited liability company – which was introduced in 2013 to encourage entrepreneurship.





Its capital may not be lower than EUR 1 or higher than EUR 9,999.99. The capital must be fully paid in cash to the governing body at the time of the company's incorporation.

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

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

No 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 outlined below.

- (i) Drafting of the memorandum of association: this records essential information about the company (notarial deed).
- (ii) Drafting of the articles of association: these contain rules for the operation and governance of the company (notarial deed).
- (iii) Registration with the local VAT office: the new company must apply for a VAT number and tax code as soon as it has been incorporated.
- (iv) Acquisition of tax codes for the directors: the members of the board of directors, if foreign, must apply for Italian tax codes.
- (v) Enrolment in the Trade Register: the company acquires legal status after registration.

The process of setting up 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.

- (i) It reaches the end of its duration, as established in its articles of association.
- (ii) The purpose for which it was established has been achieved or can no longer be achieved.
- (iii) The meeting of the shareholders/quotaholders 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 a departing 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 meeting of the shareholders/quotaholders 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 meeting of the shareholders/quotaholders fail 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 interest in the company. 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 shareholder/quotaholder resolution and, where necessary, after the cause of liquidation has been removed.

The liquidation procedure ends 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.

Representative office

A representative office – which is not a legal entity of a foreign company in Italy – is a local facility that promotes the company and its products/services and performs other non-

business operations. From a tax perspective, 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) to be covered by the foreign company's head office.

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

Branch

A branch is an extension of the foreign entity and depends – both administratively and financially – on its headquarters. It uses the same name and legal form as the foreign company. Moreover, 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 breach of the contractual obligations are directly attributable to the latter.

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





3.3 M&A transactions

3.3.1 General overview

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

- (i) share/quota deals involving the purchase of shares (S.p.A.) or quotas (S.r.l.);
- (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 of the limits on foreign investments described above.

When the turnover of the undertakings involved in the acquisition exceeds certain thresholds, prior notice of the transaction has to be given to the:

- (i) Italian Competition Authority, and/or
- (ii) European Commission.

While in most instances the choice between a share/quota deal and an asset deal will be driven by tax considerations (see below), there are several legal implications to be taken into account in structuring a transaction, and to be carefully addressed when drafting 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 its assets as well as all existing and potential liabilities and debts. It also takes over all of 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.

A change in the controlling interest of the target company does not result in a change of employer on paper, and there are no express legal obligations to notify or consult with trade unions in advance of the share/quota deal, 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, it is advisable to enter into agreements with the shareholders/quotaholders to regulate the governance of the target.

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 scope of the transaction (i.e. the assets, contracts, liabilities, workforces being transferred).

In asset deals, the following issues have to be considered.

- (i) Despite any agreements between the parties that say otherwise, the purchaser and the seller become jointly liable to creditors 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 on 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 the 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: a buyer who directly, indirectly or jointly acquires a stake of more than 30 percent in a target company listed on the Italian Stock Exchange must make a public offer or takeover bid (TOB) for the entire corporate capital of the target (a 'Mandatory TOB').

The TOB price should not be 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 not be lower than the market average over the previous 12 months.

The main steps in a Mandatory TOB are outlined below.

- (i) Announcement of the TOB: notification of the obligation to make the bid is sent immediately to CONSOB.
- (ii) Filing of the bid documents: the bid documents are submitted to CONSOB for publication (no later than 20 days after the announcement).
- (iii) Approval of the bid documents by CONSOB (within 15 days of filing).
- (iv) Immediate publication of the TOB.
- (v) The subscription period can start five days after publication and lasts between 15 and 25 days.

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

- (a) If the stake acquired is less than 90 percent: the bidder may make a further TOB for the remaining shares, with no price constraints.

- (b) If the stake acquired is 90 percent or more, but below 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 asking to sell. The squeeze-out price is set according to CONSOB rules.
- (c) If the stake acquired is 95 percent or higher: the bidder (i) must acquire the minority stake of any shareholder asking to sell; and (ii) will have the right to acquire any minority stake within three months and to delist the target. The squeeze-out price is set according to CONSOB rules.

3.4 Corporate criminal liability

Italian law includes corporate criminal liability for specific types of offences.

A company can be held responsible if the offence:

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

The crimes which may result in corporate criminal liability are detailed in the decree. They include:

- (a) offences against the public administration (such as corruption or embezzlement)
- (b) corporate crimes (such as the falsification of financial statements or prospectuses)
- (c) offences involving market abuse





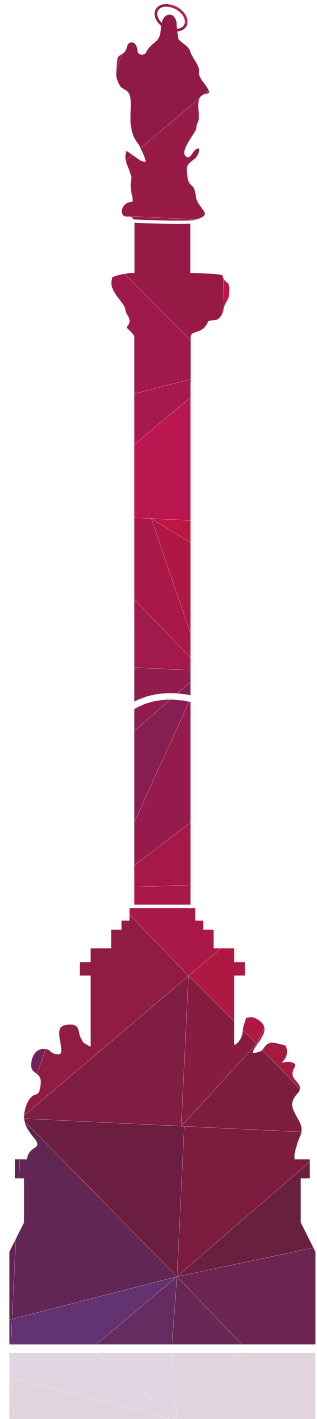
- (d) money-laundering crimes
- (e) occupational health and safety crimes
- (f) environmental crimes.

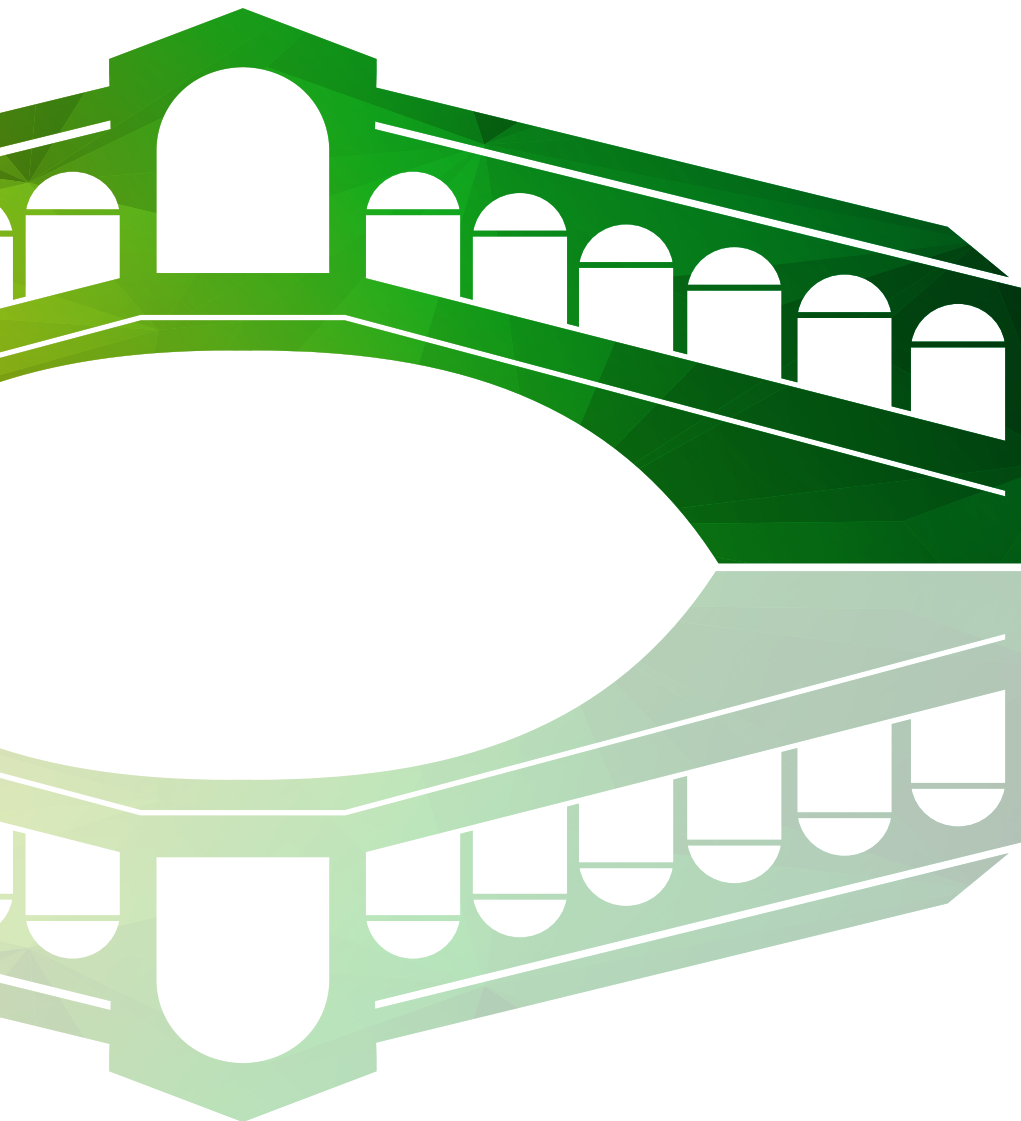
Liability may result in fines of up to EUR 1.5 million (for multiple crimes connected to the same underlying action, fines may be increased threefold, to a maximum of EUR 4.6 million) and other penalties that may endanger the survival of the company, such as:

- suspension or revocation of authorisations, licences or concessions;
- exclusion from public financing, grants or subsidies;
- a permanent operating ban.

The company may be exempted from liability if it can prove that it has adopted and effectively implemented an Organisational, Management and Control Model that (i) is capable of preventing offences, (ii) details the key areas of risk, and (iii) is supplemented by suitable disciplinary and treasury management operating procedures.

Moreover, the company must have appointed a supervisory board, selecting its members from a pool of qualified persons who come from a legal or accounting background and satisfy the requirements of independence, professionalism, ethical standards and expertise. Vested with independent powers, the duty of the supervisory board is to keep the Organisational, Management and Control Model up-to-date, monitor its effectiveness, and check that it is complied with.







4. Accounting and reporting

4.1 Legal framework and regulations

Accounting and reporting are mainly regulated by:

- the Italian Civil Code
- Italian tax codes
- Italian GAAP
- International Financial Reporting Standards, where applicable.

4.2 Requirements

In Italy the double-entry method of bookkeeping is used. Entries 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 of 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 and also show the financial year (e.g. 2017/1, 2017/2, 2017/3, etc.). Stamp duty (currently EUR 16) 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 XX' 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 law and tax law do 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. Moreover, the Italian Ministry of Finance has clarified that the accounting records of Italian companies belonging to multinational groups may be kept abroad. The accounts may be recorded and processed, in real time, using an electronic data processing system located abroad, connected to the Italian subsidiary via telephone/satellite.

However, 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 registered accounting data 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.

Invoices may be stored abroad in a digital system on condition that:

- there is a reciprocity agreement in place between the two states with regard to indirect taxation;
- the Italian company can ensure automatic access to the archive at all times from its registered office;
- the integrity and readability of the data is ensured during the whole period of storage;
- 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, P&L account, 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 Financial Reporting Standards (IFRS)

4.7.1 Differences between local GAAP and IFRS

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.

Unlisted 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 form 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 form when, for three consecutive years, they have not exceeded two of the following limits: total assets of EUR 4,400,000; revenues of EUR 8,800,000 from sales and services; 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 following table is intended solely as a way of illustrating certain notions that could be of interest and cannot be considered exhaustive.

LOCAL GAAP	IFRS
General	
<p>A statement of cash flows is required. The layout of the financial statements is indicated in company law.</p> <p>No extraordinary items are listed on the income statements. They are disclosed in the notes.</p> <p>Restatements of comparatives are not allowed. The effects of changes in accounting policies and corrections of errors are included in the income statements of the current year.</p> <p>Net equity changes only as a result of (i) actions attributable to equity holders and (ii) the profit or loss of the period.</p>	<p>A statement of cash flows is required. IFRS do not prescribe a standard format for the financial statements.</p> <p>No extraordinary items are presented in the income statements.</p> <p>Changes in accounting policies and corrections of errors could lead to restatements of comparatives.</p> <p>Net equity changes as a result of (i) actions attributable to equity holders, (ii) the profit or loss of the period, and (iii) income or expenses recognised directly as equity (other comprehensive income).</p>
Consolidation	
<p>Currently exercisable potential voting rights are not taken into consideration in identifying subsidiaries and associates.</p> <p>SPVs may be included in the consolidation when the results of the SPV could affect the investor.</p> <p>Minority interests are not part of net equity.</p> <p>Consolidation is required when two of the following limits are exceeded in two consecutive years (public interest companies are outside the scope of this rule):</p> <ul style="list-style-type: none"> • Total assets: EUR 20 million • Total revenue: EUR 40 million • 250 employees. 	<p>An entity is consolidated when it is considered to be under the control of another.</p> <p>Having control is defined as having the power to control the assets of an entity and being exposed to the results of that entity.</p> <p>In identifying subsidiaries and associates, the existence of currently exercisable potential voting rights is taken into consideration.</p> <p>SPVs are considered to be controlled entities when the investor is exposed to fluctuations in the SPV's results; there is no specific threshold.</p>





LOCAL GAAP	IFRS
ASSETS	
Acquired intangible assets	
<p>All intangible fixed assets are amortised and some have a maximum useful life of five years. Start-up costs (e.g. training) and the cost of issuing shares can be capitalised, with certain restrictions.</p> <p>Advertising costs may not be capitalised.</p> <p>Goodwill arising from a business combination is amortised over its useful life. The amortisation period cannot be longer than ten years by law (Italian GAAP allow this period to be extended to a maximum of 20 years in certain cases).</p> <p>Revaluations are not permitted unless authorised by special laws.</p>	<p>If the criteria for capitalisation are satisfied, intangible assets must be amortised over their estimated useful life. The cost of issuing shares is recognised as a deduction from equity.</p> <p>Goodwill arising from a business combination and intangible assets with an indefinite useful life are not amortised but subject to an impairment test at least once a year.</p> <p>Revaluations are possible in very few cases.</p>
Internally generated intangible assets	
<p>Research costs may not be capitalised.</p> <p>There is the option of capitalising and amortising development costs if certain conditions are satisfied.</p>	<p>Research costs are charged when incurred. Development costs are capitalised and amortised when rigorous criteria are satisfied.</p>
Property, plant and equipment	
<p>These must be stated at their historical cost.</p> <p>Revaluations are not permitted unless authorised by special laws.</p>	<p>These are measured using either the cost model or the revaluation model. When the revaluation model is used, the entire category of assets has to be revaluated with sufficient regularity.</p>
Leases (as lessee)	
<p>All leases are recognised in the financial statements as operating leases. Disclosures are required by law for financial leases.</p>	<p>Financial leases are recognised in the financial statements on the basis of substance rather than form.</p>
Investment properties	
<p>These must be stated at cost and depreciated over their useful life. Fair value is not permitted.</p>	<p>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.</p>
Inventories	
<p>Similar to IFRS, although the FIFO, LIFO and Weighted Average Cost methods are allowed.</p>	<p>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.</p>





LOCAL GAAP	IFRS
Financial assets (measurement and derecognition)	
<p>Long-term investments are recognised at the cost of acquisition. When this cost is permanently impaired, they are recognised at their lower value.</p> <p>Short-term investments are recognised at the cost of acquisition. They are valued at the lower of cost of acquisition and market value.</p> <p>Loans and receivables with a reduced and favourable interest rate are recognised at their amortised cost.</p> <p>There is no guidance on derecognition, which is generally based on loss of legal ownership.</p>	<p>Measurement of financial assets depends on their classification and may be at:</p> <ul style="list-style-type: none"> – their amortised cost (held-to-maturity assets, loans and receivables); – their fair value through equity (financial assets available for sale); – their fair value through profit or loss (financial assets not included in the above categories). <p>The derecognition of financial assets is mainly based on the transfer of risk and rewards.</p>
Hedging derivatives instruments	
<p>Specific guidance is provided by OIC Standard 32 on the definition and valuation of hedging derivatives and the information required in the statutory financial statements.</p> <p>All derivative instruments are measured at their fair value.</p> <p>Fair value hedges have different representation criteria to cash flow hedges.</p>	<p>All derivative instruments are measured at fair value. Any change in fair value is recognised in income statements, except for effective cash flow hedges, where the changes are deferred in equity until the effect of the underlying transaction is recognised in the income statement.</p>
LIABILITIES AND EQUITY	
Financial liabilities and equity instruments (classification)	
<p>Classification is based on the legal form of the financial instruments.</p> <p>Preference shares are always included in equity.</p> <p>Convertible debt is always recognised as a financial liability.</p> <p>Purchased own shares are recognised as a deduction from equity.</p>	<p>Classification depends on the substance of the issuer's obligations.</p> <p>Mandatorily redeemable preference shares are classified as financial liabilities.</p> <p>Proceeds received as a result of issuing convertible debt are allocated between equity and financial liabilities.</p> <p>Purchased own shares are recognised as a deduction from equity.</p>
Restructuring provision	
<p>A restructuring provision is recognised at the moment of the board of directors' resolution.</p>	<p>A restructuring provision must be made if a detailed plan has been announced or if the implementation of a plan has actually started.</p>





LOCAL GAAP	IFRS
INCOME STATEMENTS	
Revenue	
OIC Standard 12 provides guidelines on revenue recognition. Revenues are generally recognised when ownership is transferred or when revenue is legally enforceable.	Based on several criteria, which require the recognition of revenue when risks and rewards have been transferred and the revenue can be measured reliably.
Employee benefits – pension costs (defined benefit plans)	
There is no binding guidance on pension costs. An actuarial calculation may be used in calculating the amount to be set aside for TFR when the amount is a large one and long-term planning is important.	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 year-end financial statements (including notes) by adopting a specific resolution during a general meeting convened in accordance with the company's articles of association.	Within 120 days of the year end (180 days in special circumstances).
2.	Filing of the annual financial statements.	The financial statements (including the notes) and the minutes of the shareholders' meeting must be filed in electronic 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 by adding details of the assets and liabilities shown in the annual financial statements.	Within three months of the annual <i>Redditi</i> SC return filing date.





4.8.2 Tax returns and tax payments

	Task	Description	Deadline
1.	Filing of certificates of income subject to WHT.	The certificates must be sent electronically or by recorded delivery letter to every local payee (e.g. agents, professionals, employees) and every non-resident entity that has received payments of royalties, interest or dividends. The certificates must be sent in electronic format to the Revenue Agency.	7 March to the payee 31 March to the Revenue Agency
2.	Payment of the annual duty on accounting records.	A duty of EUR 309.87 must be paid if the share/quota capital is lower than EUR 516,456.90; otherwise the duty is EUR 516.46.	16 March
3.	Payment of any remaining VAT not paid by the monthly due dates during the previous calendar year.	The difference between output and input VAT is payable on the 16th of each subsequent month. Late payments are subject to fines.	16 March
4.	Filing of the annual VAT return for the previous calendar year.	No late filings are allowed.	30 April
5.	Payment of the balance of income taxes (IRES + IRAP) for the financial year ending 31 December.	The income taxes payable are net of the advances due by 30 June and by 30 November of the previous financial year.	30 June
6.	Payment of the annual Trade Register charge.	Payment is due on the same date as payment of the balance of income taxes. The amount is decided by the Chamber of Commerce and published in advance.	30 June
7.	Filing of the annual 770 withholding tax return.	The annual 770 withholding tax return for WHT must be filed electronically.	31 October
8.	Filing of the <i>Redditi</i> SC return and the IRAP return for the year ending 31 December.	The <i>Redditi</i> SC return and the IRAP return must both be filed electronically.	31 October
9.	Payment of the advance VAT due for December.	When applicable, and based on the historical method, the advance VAT due is 88 percent of the VAT paid in December of the previous year.	27 December
10.	Monthly VAT reporting of the details of sale and purchase invoices issued to or received from companies not established in Italy	The data must be filed electronically using special software.	Monthly
11.	Quarterly VAT reporting of periodic settlement data.	The details must be filed electronically using special software. Data on periodic VAT payments must be included. The due dates for 2019 are: – 31 May 2019 for Q1 – 16 September 2019 for Q2 – 30 November 2019 for Q3 – 29 February 2020 for Q4.	Quarterly





4.9 Failure to keep accounting books and records properly

Failure to keep accounting records is punishable by fines ranging, for the period up to 31 December 2016, from EUR 1,032 to EUR 7,746 and, as of 1 January 2017, from EUR 1,000 to EUR 8,000. Fines are doubled if, in any financial 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 from 1 January 2017.

If the company fails to keep accounting books and records in an attempt to conceal profits or turnover, the legal representative is liable to criminal prosecution.

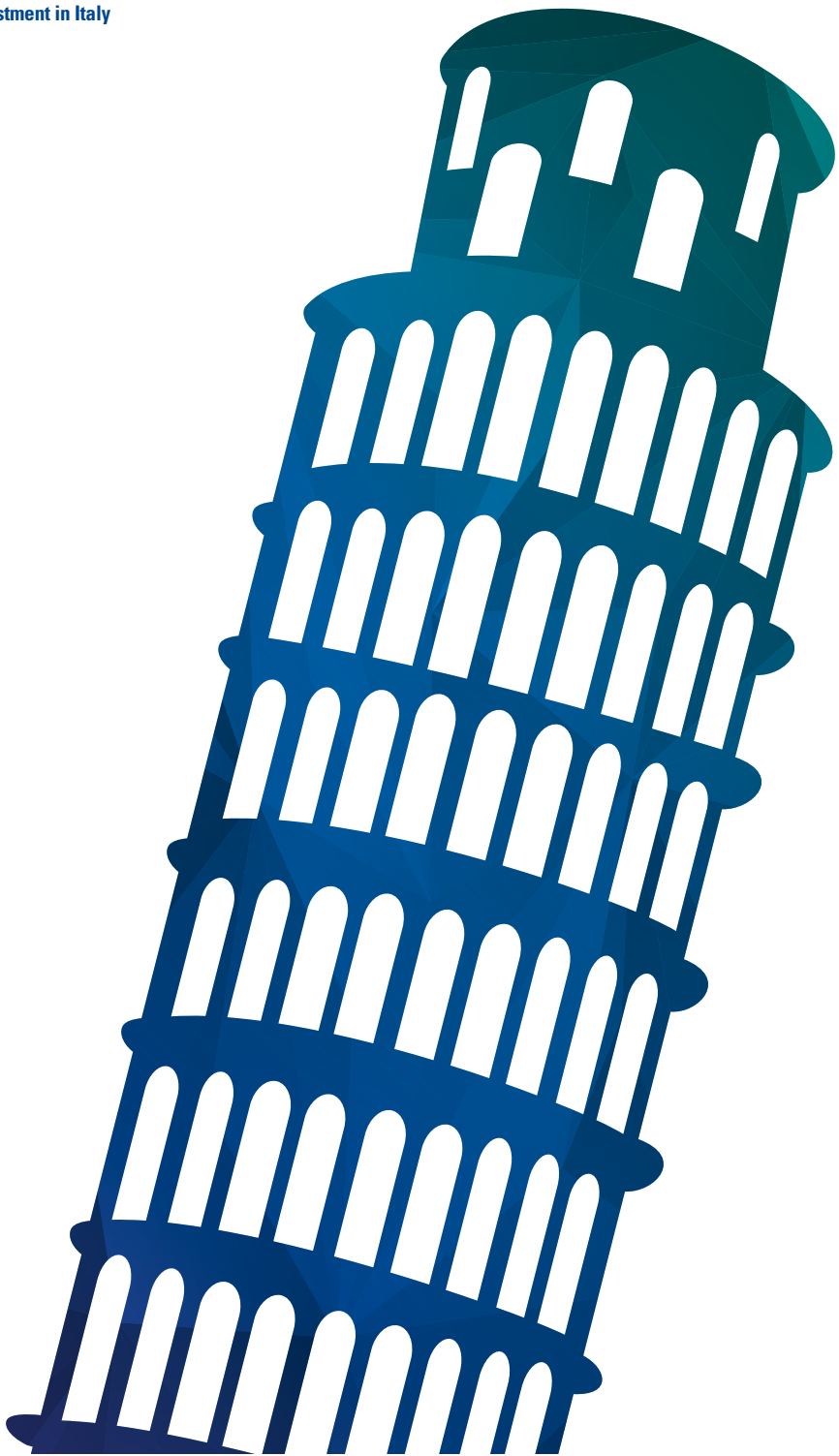
Upon the incorporation of a company, the tax authorities must be informed of where the accounting books and records are kept and may be accessed during tax inspections. Any subsequent changes must also be reported accordingly.

As explained above, bookkeeping abroad is allowed on 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.

4.10 Electronic invoicing

Starting from 1 January 2019, invoices for all B2B transactions must be issued electronically and transmitted via the SDI.







5. Taxation of business income

5.1 Domestic aspects

BASIC TAX FACTS	
Corporate tax rate	24% (IRES) + 3.9% (IRAP)
Limits on interest deduction	Yes (earning stripping rule)
Rules on dormant companies	Yes
Patent Box regime	Yes
Loss relief (carryforward/carryback)	Carryforward
Capital gains tax rate	26%/0%
Participation Exemption	Yes (95% exemption)
Domestic WHT rate on dividends paid to non-residents	26%/1.2%
Domestic WHT rate on interest paid to non-residents	26%/12.5%/5%/0%
Domestic WHT rate on royalties paid to non-residents	30%/22.5%
Number of countries with which Italy has a DTT	96
Double taxation relief for dividend income from controlled subsidiaries (tax with credit/exemption)	Exemption (95%)
Double taxation relief on income derived from a foreign permanent establishment (foreign tax credit/exemption)	Foreign tax credit; exemption (optional) under certain 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 financial year.

Resident companies are taxed on their worldwide income, while non-residents are only taxed on their Italian income.

5.1.2 Tax 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 IRAP base is normally different from the IRES base.

The compound tax rate is therefore approximately 27.9 percent, whilst the effective rate may be very different.

5.1.3 Calculation of taxable income

For IRES purposes

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.

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 CIT purposes and prevail over any provisions contained in the ITC.

Many of the rules applicable to IAS/IFRS adopters are extended to companies that adopt local GAAP, e.g. certain rules on financial instruments and derivatives.

For IRAP purposes

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

The labour costs of employees on 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, 10 percent of the IRAP payment is deductible for IRES purposes, provided that the company has incurred interest expense during the financial year concerned. Furthermore, IRAP paid on any non-deductible labour costs is deductible from the IRES 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 low-tax jurisdiction⁶ and (ii) not allowed to deduct the dividend distribution⁷.

One hundred percent of the dividends received by a resident taxpayer from an affiliate located or operating in a CFC low-tax jurisdiction are subject to IRES in Italy – whether the dividends are received directly, or indirectly through a controlled company located in Italy or in a jurisdiction that is not a CFC low-tax jurisdiction.

Dividends are deemed to arise in a low-tax jurisdiction and are therefore 100 percent taxable to the resident shareholder if:

1. in the case of direct or indirect controlling interests (as defined for the purposes of the CFC rule⁸), the controlled company has an effective tax rate that is lower than 50 percent of the tax rate that would apply if it were resident in Italy;
2. in the case of other equity interests, the investee company is subject to a nominal tax rate that is lower than 50 percent of the domestic one (or to a special regime that leads to the same result).

The resident shareholder may avoid full taxation if one of the following two safe-harbour rules applies.

1. The taxpayer is able to prove that an actual business is carried out in the foreign jurisdiction through local personnel, equipment, other assets and premises (CFC safe-harbour rule⁹). This leads to a 50 percent dividend exemption (and a foreign tax credit in the case of controlling interests).

2. The taxpayer is able to prove that the investment in the foreign entity does not shift income to a low-tax jurisdiction (subject-to-tax requirement). This leads to the standard 95 percent exemption.

The taxpayer can submit an application for a tax ruling to understand whether the above safe-harbour rules may apply.

Capital gains earned by resident companies on the transfer of shares

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 – and 95 percent of capital losses earned from the transfer of shares are not deductible - 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 cooperative jurisdiction (or an advance ruling is obtained, confirming that the company directly produced most of its taxable income in a cooperative jurisdiction).

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

Normally write-offs, losses and step-ups in the tax basis of shares are not tax-relevant.

⁶ See the section headed 'Controlled foreign company rule' in 5.3 below.

⁷ In the case of dividends paid to an Italian parent by an EU subsidiary eligible for the Parent-Subsidiary Directive, 95 percent of the dividends that cannot be deducted by the subsidiary are exempt from tax in the hands of the Italian parent. Therefore, only the portion that can be deducted by the subsidiary is taxed in Italy.

⁸ See the section headed 'Controlled foreign company rule' in 5.3 below.

⁹ See the section headed 'Controlled foreign company rule' in 5.3 below.





Occasionally, however, temporary rules have been issued, allowing step-ups against payment of substitute tax. Occasionally, however, temporary rules have been issued, allowing step-ups against payment of substitute tax.

Capital gains earned by resident companies on the transfer of shares held in entities located in low-tax jurisdictions

Until 2018, capital gains from the transfer of shares in entities located in a low-tax jurisdiction (outside the EEA) were 100 percent taxable to the resident seller, unless the subject-to-tax requirement had been met **ever since** it had held the shares. A very recent legislative decree¹⁰ has modified the above rule with effect from the financial year subsequent to that in progress on 31 December 2018. The new rule establishes that if the purchaser does not belong to the same group as the seller (i.e. does not control, is not controlled by and is not under the same control as the seller) the subject-to-tax requirement has to be met over the previous **five years only**, in order to benefit from the Participation Exemption regime.

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 the 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 below. 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, 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 516.46 it may be fully deducted in the year of purchase.

Amortisation of intangible assets

Patents and know-how: up to 50 percent of the cost of the asset can be deducted in each financial 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 financial 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 5 percent of the gross value of the depreciable tangible assets at the beginning of the financial year.

¹⁰ The legislative decree of 28 November 2018, by which the Italian government has implemented the EU Anti-Tax-Avoidance Directives.





Any remaining costs may be deducted over the following five financial 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 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 (the portion of interest expense exceeding interest income) can be deducted to the extent of 30 percent of EBITDA (gross operating income). A very recent legislative decree¹¹ has modified the deductibility of interest expense with effect from the financial year subsequent to that in progress on 31 December 2018. EBITDA is still 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; however, reference should now be made to the tax bases of these items, calculated in accordance with tax rules (previously EBITDA had to be calculated on the basis of the book values of the items). 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 financial years against any prior excess interest income, or against EBITDA to the extent that the net interest expense accrued in those subsequent

years is less than 30 percent of EBITDA. If, in a given financial year, the 30 percent of EBITDA is higher than the net interest expense, the surplus may be carried forward over the following five years (before the amendments, excess EBITDA could be carried forward indefinitely) and used to increase the EBITDA available in subsequent years. The EBITDA excess capacity must be offset on a FIFO basis.

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 not been allowed.

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

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 financial 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 a receivable that is not

¹¹ See footnote 10 on p. 52.





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 of provisions are not 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.

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 losses are deductible in the financial 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 financial year in which they must be derecognised in accordance with the relevant accounting standards, such credit losses cannot be deducted.

5.1.6 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 three years of business, which can be offset against 100 percent of the taxable income of any future year until they are used up.

Carryforward 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 financial years when it incurred the losses (this change is significant if it occurs in the financial year of the transfer or the two previous or subsequent years).

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

If they originate during a consolidation period, tax losses can be transferred to the parent of a tax group to offset income produced by the parent or other group companies. 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).





5.1.7 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:
 - (i) 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 financial 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 financial 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 financial 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 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 terminated 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 participants.

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, condition (iii) was 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. Therefore, companies resident in Italy can be consolidated for tax purposes if they are controlled by a foreign company that is resident in a treaty country and that pursues its activity in Italy through a permanent establishment, even if that permanent establishment does not hold the shares in the Italian subsidiary.

Moreover, companies resident in Italy can be consolidated for tax purposes if they are controlled by a foreign company that is resident in an EU/EEA cooperative jurisdiction and has no permanent establishment in Italy. Permanent establishments, in Italy or in an EU/EEA cooperative jurisdiction, of controlled companies resident in another EU/EEA cooperative jurisdiction can also be consolidated. This form of consolidation requires the non-resident controlling entity to appoint an Italian (or EU/EEA) controlled company as the consolidating entity of the sub-group.





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
- (ii) controlled by the government, by a governmental entity, or by Italian-resident 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 financial 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 Revenue Agency, 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 unless the participants opt out.

Under the worldwide consolidation regime, the income of each non-resident 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.

5.1.8 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. Qualifying companies are those whose shareholders are all corporates, holding an interest of between 10 percent and 50 percent in the profits and in the voting rights of the company. 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 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.

5.1.9 New tax on digital services (web tax)

The 2019 Budget Law introduces a 3 percent web tax that will apply to revenues generated from certain digital services rendered to Italian B2B and B2C customers by companies or groups of companies of a certain size, regardless of their place of residence.

The web tax will apply to businesses that, individually or group-wide, generate both of the following during a calendar year:

- a) total revenues of not less than EUR 750 million, wherever realised;





- b) revenues of not less than EUR 5.5 million, realised in Italy from the digital services defined below.

The tax will apply to revenues derived from the provision of the following services:

- a) the transmission, on a digital platform, of advertising targeted at users of that platform;
- b) the availability of a multilateral digital platform that enables users to enter into contact and interact with each other, also in order to facilitate the direct supply of goods and services;
- c) the transmission of data collected from users and generated by the use of a digital platform.

Revenues derived from the provision of the above services will not be taxable if the services are rendered to companies that are deemed to be parent, subsidiary or sister companies.

Non-established parties that do not have a permanent establishment in Italy or an Italian VAT number, and that qualify as taxable persons, must obtain an identification number for web tax purposes by submitting an application to the Italian Revenue Agency.

The government should issue a web tax implementing decree by 30 April 2019 and the web tax rules should become effective 60 days after its publication, i.e. from 30 June 2019.

This web tax legislation repeals the rules that were introduced by the 2018 Budget Law but never came into effect.

5.1.10 Incentives

Reduced 15 percent IRES rate

The 2019 Budget Law provides that, from the financial year subsequent to that in progress on 31 December 2018, companies meeting certain requirements will benefit from a reduction of the standard 24 percent IRES rate by nine percentage points on a portion of their income.

More specifically, a reduced 15 percent IRES rate will apply to a portion of income computed on the lower of the following:

- (i) the previous financial year's profits (i.e. FY 2018) set aside to balance sheet reserves (other than non-distributable reserves);
- (ii) total investments in new fixed assets and new personnel hired on fixed-term or permanent contracts.

Patent Box

Since the financial year following that in progress on 31 December 2014, entrepreneurs resident in Italy, or Italian permanent establishments of entities resident in countries that have signed a DTT and exchange information with Italy, have been able to 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 (currently software protected by copyright, patents, designs, models, processes, secret formulas and industrial, commercial or scientific knowledge, including know-how). The percentage of qualifying income that is not included in the IRES or IRAP base was 30 percent for 2015 and 40 percent for 2016, and is 50 percent as of 2017 (for calendar-year taxpayers). Once it has been opted for, the arrangement is irrevocable and remains in place for five 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 financial year following that of the asset transfer.

IP income covered by the regime must be determined on the basis of OECD international standards, in particular the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations.

To align Italian tax law with the OECD guidelines contained in the final Report on BEPS Action 5, trademarks - originally included - have been removed from the list of qualifying intangibles. The disqualification of trademarks applies to taxpayers who opt for the Patent Box regime after 31 December 2016 (i.e. for calendar-year taxpayers, the benefit is not available for income attributable to trademarks from 2017). Options exercised with respect to trademarks in financial years in progress on 31 December 2015 or 31 December 2016 have been grandfathered and will remain valid until their natural deadlines (2019 and 2020, respectively) or, at the latest, 30 June 2021.

R&D tax credit

The 2019 Budget Law modifies 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

financial years preceding that in progress on 31 December 2015 (2012, 2013 and 2014 for calendar-year taxpayers).

The tax credit is in general 25 percent of the difference in spending, rising to 50 percent for certain R&D costs only (mainly the cost of employees assigned to R&D, or costs arising from contracts with universities, research bodies, start-ups established in Italy, and innovative SMEs). The tax credit is capped at EUR 10 million per year for each beneficiary.

The R&D tax credit can be used only if specific formalities are complied with. The 2019 Budget Law adds a new obligation to the mandatory certification requirements: a detailed technical report describing the purposes and results of the R&D must be prepared and kept by the tax credit recipient.

The amendments to the R&D tax credit rules will apply from the financial year following that in progress on 31 December 2018, i.e. from 2019 for calendar-year taxpayers. However, the new technical report is required retroactively, from the financial year in progress on 31 December 2018.

For the computation of the R&D tax credit, the 2019 Budget Law officially clarifies that only R&D carried out directly in laboratories or facilities established in Italy qualifies.

The R&D tax credit is also available for research centres which are established in Italy and develop IP on behalf of foreign companies.

Allowance for corporate equity (ACE)

The rule in place until 31 December 2018 allowed a deduction from the total IRES base of an amount corresponding to notional interest on the increase in new equity since 31 December 2010. ACE applied after computation of the total net income, already net of any tax losses. If the amount of notional interest exceeded the total net income, the surplus could be carried forward, in full and indefinitely, to subsequent financial years, to be deducted from the first available taxable income.





The Budget Law 2019 repeals ACE from 1 January 2019. Thus, for calendar-year taxpayers, FY 2018 will be the last year in which it applies (at a rate of 1.5 percent).

Any notional interest exceeding the total net income of the financial year ended on 31 December 2018 may be carried forward to be deducted in subsequent financial years or converted (in whole or in part) into a tax credit, to be used - in five equal annual instalments - exclusively to reduce IRAP payments.

Extra depreciation

The extra depreciation regime introduced by the 2016 Stability Law and renewed for FY 2018 has not been extended to FY 2019.

Hyper depreciation

The 2019 Budget Law extends the hyper depreciation regime (introduced by the 2017 Budget Law) to investments made in 2019 in tangible assets to be used in production facilities located in Italy, in the technological and digital development of enterprises covered by the Industry 4.0 Plan promoted by the Italian government. As a general principle, all conditions and rules applicable to investments made in financial year 2018 will be applicable to investments made in financial year 2019. Moreover, the hyper depreciation regime will also apply until 31 December 2020 provided that, by the end of 2019:

- the seller has accepted the purchase order, and
- at least 20 percent of the purchase cost has been paid in advance.

Previously, the purchase cost of eligible tangible assets could be increased by 150 percent. Under the 2019 Budget Law, this rule has been replaced by three different percentages:

- 170 percent for investments of up to EUR 2.5 million
- 100 percent for investments ranging from EUR 2.5 million to EUR 10 million

- 50 percent for investments ranging from EUR 10 million to EUR 20 million.

On the same terms as in the past, there is extra amortisation of investments in intangible assets made by taxpayers that also use hyper depreciation for tangible assets in 2019 (and in 2020 if the above two conditions are met). The purchase cost of the intangible assets can be increased by 40 percent.

The eligible costs now include fees paid to access intangibles through cloud computing systems. In this case the benefit can only be taken, on an accruals basis, in respect of the fees charged to the relevant year.

To obtain the benefit, the legal representative of the company must provide a self-declaration or, if the purchase cost of the asset exceeds EUR 500,000, a technical appraisal to confirm that the asset meets the requirements.

Other incentives

Other tax incentives are available for companies that invest in innovative start-ups or SMEs, for companies that provide employee training leading to qualifications, and for SMEs that purchase consultancy services for the listing of their shares.

Tax credits for specific expenses

There are several benefits granted to companies in the form of a tax credit for expenses incurred in specific sectors/regions or for specific purposes that the legislators wish to incentivise, e.g. agriculture, disadvantaged areas in southern Italy, improved energy efficiency.





5.1.11 Taxable income of partnerships

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 non-resident partner has no permanent establishment in Italy.

5.2 International aspects

5.2.1 Withholding taxes

5.2.1.1 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 pension funds set up in cooperative jurisdictions¹² (with no 11/26 tax credit refund).

The above rates may be reduced under DTTs.

Parent-Subsidiary Directive

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 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).

The general anti-avoidance rule applies (see section 5.3.1 below).

By the dividend payment date, the beneficial owner must submit a form to the payer (the WHT agent) in order to benefit directly 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 cooperative jurisdiction may be subject to a reduced 1.2 percent domestic WHT (the same level of taxation applied to dividends received by domestic parent companies).

The Agreement of 26 October 2004 between the European Union and Switzerland

Under article 15 of this agreement, Italy must exempt dividend payments to companies resident in Switzerland under essentially the same conditions as those laid down in the version of the Parent-Subsidiary Directive in force before 1 January 2005. The conditions are listed below.

- The parent must have directly held at least 25 percent of the subsidiary's equity for at least two years.
- One company must be resident for tax

¹² As defined in the glossary.





purposes in Italy and the other company must be resident for tax purposes in Switzerland.

- Under any DTTs with third states, neither company must be resident for tax purposes in that third state.
- Both companies must be fully subject to CIT, without benefitting from exemptions.
- Each company must be a corporation.

5.2.1.2 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 DTTs. 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 'Exemption under the 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:

- (i) all the exemption requirements established by the Interest and 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 cooperative jurisdiction;
- (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).

Exemption on interest paid on qualifying bonds to a foreign taxpayer established in a cooperative jurisdiction

Interest and similar proceeds (e.g. issue discounts) are exempt from WHT 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 cooperative jurisdiction, whether or not it is subject to tax (these residents may include institutional investors such as investment funds).
- b) Interest accrues on, inter alia, the following assets: (i) Italian bonds and treasury bonds of cooperative jurisdictions; (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 cooperative EEA jurisdiction; (iii) notes issued by securitisation vehicles. In certain cases, interest on bonds, bond-like securities and commercial papers issued by unlisted 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.

Exemption on interest on cross-border loans

The WHT 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 cooperative jurisdiction (e.g. an investment fund).





Royalties

Generally, a 30 percent final WHT is levied on royalties paid by a resident taxpayer (including a permanent establishment in Italy of a non-resident) to a non-resident taxpayer. The definition of royalties is broadly in line with the one provided by the Commentary on the OECD Model Tax Convention. If the non-resident recipient of the royalties has acquired the IP for a consideration, the tax base is reduced to 75 percent of the gross amount of the royalties, i.e. 22.5 percent of the effective WHT rate. There is no WHT on royalty payments to Italian permanent establishments of non-resident entities. The WHT may be reduced or eliminated under DTTs or the Interest and Royalties Directive (see below).

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.

By the payment date, the beneficial owner must submit a form to the payer (the WHT agent) in order to directly benefit from the exemption.

Exemption under the Agreement of 26 October 2004 between the European Union and Switzerland

Under article 15 of this agreement, outbound interest and royalty payments to companies resident in Switzerland are exempt under essentially the same conditions as those laid down in the Interest and Royalties Directive in force before 1 January 2005. However, the holding period is two years instead of one and a 25 percent equity holding is required instead of voting rights.

5.2.2 Permanent establishments

Definition of permanent establishment

Under the domestic definition, a permanent establishment for IRES and IRAP purposes is a fixed place of business through which the business of a non-resident enterprise is wholly or partly carried on in Italy.

The 2018 Budget Law broadened the domestic permanent establishment definition, with effect from 2018, in order to make it fully consistent with that proposed by the OECD in the BEPS Action 7 Final Report and the 2017 OECD Commentary on the OECD Model Tax Convention.

These changes to the domestic permanent establishment definition will need to be coordinated with Italy's position on the





Multilateral Instrument (MLI)¹³: Italy, for instance, reserved the right not to broaden the agency permanent establishment definition (see section 5.2.7).

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 the activity is (a) included in the 'negative' list (i.e. cases when an activity does not give rise to a fixed-place permanent establishment) and (b) used only to perform certain preparatory or auxiliary activities. This second condition must be proved by the taxpayer.

The 2018 Budget Law also introduced an additional definition of fixed-place permanent establishment, as a "significant and continuous economic presence in the territory of Italy, built in such a way that it will not result in a physical presence in Italy": a so-called 'digital permanent establishment'. From 2018 on, the installation in Italy of computers or similar systems that allow electronic collection and delivery of data may therefore give rise to a fixed-place permanent establishment.

The new definition of fixed-place permanent establishment also includes an anti-fragmentation rule, which means that in conducting tax audits to ascertain the possible existence of a permanent establishment, Italian tax officers must scrutinize each single activity carried on by all the group companies in Italy, even through entities that are not formally set up or identified there for tax purposes. Business processes and functions that are integrated with each other must be grouped together and the preparatory/auxiliary character of the combination of activities must be evaluated.

As of 2018, a resident or non-resident person that, in the name of a non-resident enterprise, habitually concludes contracts in Italy or operates for the conclusion of contracts (other than for the purchase of goods) with no material modifications by the non-resident enterprise 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 2018 Budget Law also altered the extent to which an agent must be independent, legally and economically, in order to exclude an agency permanent establishment. Persons who operate exclusively or almost exclusively on behalf of one or more enterprises to which they are closely related can no longer be considered independent.

The domestic definition of permanent establishment is now basically consistent with the definition given by the 2017 OECD Model Tax Convention.

Cooperation and enhanced collaboration for multinational enterprises

In 2017 a special rule for MNEs was introduced, whereby certain non-resident enterprises may apply to the Italian Revenue Agency for a ruling, in order to (i) verify whether their business activities in Italy may trigger a permanent establishment, or (ii) voluntarily disclose the existence of a previously unreported permanent establishment. If a permanent establishment is deemed to exist, the applicant can follow a settlement procedure for the open financial years, paying the additional taxes and interest due, but lower penalties.

¹³ OECD Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting.





No criminal consequences will ensue and, as an additional benefit, the applicant can automatically access the Italian cooperative compliance regime (see the section headed 'Ordinary tax rulings' in section 11.1).

Non-resident enterprises eligible to apply for a tax ruling are those that (i) belong to groups whose worldwide consolidated annual revenues top EUR 1 billion, and (ii) have annual sales of over EUR 50 million in Italy, obtained with the support of Italian entities belonging to the same group.

Though it seemed from the preparatory work within Parliament that the rule was meant to apply to enterprises in the digital economy, the final version is not narrowly worded and should also apply to industries operating outside the digital economy.

Measures implementing this rule have not yet been issued; therefore, it is not yet applicable.

Determination of taxable income

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 Tax 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, also taking into account the 2018 OECD additional guidance 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.

5.2.3 The branch-exemption regime

A 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 qualify as CFCs (see the 'Controlled foreign company rule' in section 5.3.2 below), the branch exemption will not apply and the income of such branches will be allocated to the Italian headquarters like CFC income. By contrast, if such CFC branches comply with the safe-harbour rule (again, see the 'Controlled foreign company rule' in section 5.3.2 below), the branch exemption remains available. Certain claw-back rules apply if such branches are loss-making before the election is made.

5.2.4 Foreign tax credit

If certain conditions are met, taxes paid on foreign business income could be 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 DTTs. Some treaties 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 eight years.

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 DTT with Italy. Uncertain cases should be cleared in advance with the Italian Revenue Agency.

5.2.5 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 rules established for each category of income (capital income, real estate income, etc.). Only if the non-resident partnership has a permanent establishment in Italy will the income generated by the permanent establishment be considered (and calculated) as business income.

5.2.6 Capital gains earned by non-resident companies on the transfer of shares held in an Italian company

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 a DTT applies, capital gains are usually taxable only in the seller's country of residence.
- 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 (a qualifying share), the capital gains realised by non-residents are subject to a 26 percent final WHT, like those realised on the sale of non-qualifying shares in unlisted resident companies (see below).
- 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 (a non-qualifying share), the capital gains are subject to a 26 percent final WHT. Residents of cooperative jurisdictions 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 (a non-qualifying share), the capital gain is not regarded as Italian 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 (a qualifying share), the capital gains are subject to a 26 percent final WHT.

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 gain 2019	Tax rate 2019
Unlisted	>20% voting rights or >25% capital (qualifying)	100%	26% (final WHT)
	20% or less of voting rights; 25% or less of capital (non-qualifying)	100%	26% (final WHT); zero if the investor is resident in a cooperative jurisdiction.
Listed	>2% voting rights or >5% of capital (qualifying)	100%	26%
	2% or less of voting rights or 5% or less of capital (non-qualifying)	Not regarded as Italian income	Not regarded as Italian income

5.2.7 Double tax treaties

Italy currently has 96 DTTs in force¹⁴. Under article 169 ITC, the provisions of the DTTs prevail over those of domestic law, unless the latter are more favourable to taxpayers.

On 7 June 2017 Italy signed the OECD MLI, in order to amend the DTTs in compliance with the OECD guidelines contained in the BEPS Reports¹⁵.

The MLI must be ratified through a law approved by the Italian Parliament and published in the Official Gazette. However, no official announcements have yet been made as to the steps and timing of ratification. Therefore, at present, the provisions of the DTTs currently in force still apply.

The main positions¹⁶ expressed by Italy on the MLI are the following¹⁷.

Covered Tax Agreements

Italy applies the MLI to 84 DTTs (including certain DTTs that are not yet in force, such as that with Kenya) out of the 96 currently in force. These 84 DTTs are the 'Covered Tax Agreements'.

Hybrid mismatches (Action 2)

Italy has decided to opt out of the main provisions regarding hybrid entities.

Prevention of treaty abuse (Action 6)

Italy has opted for the principal purpose test or 'PPT' rule, either by accepting the default rule, or by opting out on the basis of an existing PPT.

¹⁴ See the Ministry of Finance's website: <http://www.finanze.it/opencms/it/fiscalita-comunitaria-e-internazionale/convenzioni-e-accordi/convenzioni-per-evitare-le-doppie-imposizioni/>.

¹⁵ The 15 reports issued by the OECD on 5 October 2015, which contain measures aimed at tackling BEPS. The final reports are available at the following link: <http://www.oecd.org/tax/beps-2015-final-reports.htm>.

¹⁶ Under the provisions of the MLI, each signing jurisdiction was required to provide a list of reservations and notifications (the 'MLI Position') at the time of signature. As clarified by the OECD, a reservation made by a Contracting Jurisdiction with respect to a provision generally blocks the application of the provision, whether or not the other Contracting Jurisdiction has also made the reservation. By contrast, both Contracting Jurisdictions are required to choose to apply the same optional provision in order to apply the provision.

¹⁷ The text of Italy's MLI Position is available at the following link: <http://www.oecd.org/tax/treaties/beps-ml-position-italy.pdf>.



Permanent establishment (Action 7)

Artificial avoidance of permanent establishment status through commissionaire arrangements and similar strategies (article 12 of the MLI)

Italy reserves the right for the entirety of article 12 not to apply to its Covered Tax Agreements and has therefore decided not to amend the agency permanent establishment in compliance with Action 7 in its DTTs¹⁸.

Artificial avoidance of permanent establishment status through the specific activity exemptions (article 13 of the MLI)

Italy has chosen to apply Option A under article 13(1) of the MLI and has therefore decided to make the list of exemptions, present in all the 84 Covered Tax Agreements, subject to the further condition that they must have a preparatory or auxiliary character.

Italy has elected to include the anti-fragmentation rule, contained in article 13(4) of the MLI, in its Covered Tax Agreements.

Splitting-up of contracts (article 14 of the MLI)

Italy reserves the right for the entirety of article 14 not to apply to its Covered Tax Agreements.

Definition of a person closely related to an enterprise (article 15 of the MLI)

With respect to the anti-fragmentation rule, Italy applies the (very wide) definition of closely related enterprise contained in the BEPS Action 7 Final Report¹⁹.

Mandatory binding arbitration (Action 14)

Italy has chosen to adopt the 'mandatory binding arbitration' provision to improve dispute resolution.

5.3 Anti-avoidance measures

5.3.1 General anti-avoidance rule

The legal definition of abuse of law, which incorporates the concept of tax avoidance, is to be found in the Taxpayers' Charter²⁰.

The definition 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. In other words, 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 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.

There are certain procedures that the Italian Revenue Agency must follow. For example, the assessment notice must be preceded by a clarification request, and the taxpayer has 60 days to answer the request.

¹⁸ However, it has implemented Action 7 in its domestic rule (see above).

¹⁹ This was also included in the ITC.

²⁰ Law no. 212/2000 ('Statuto del contribuente').





The Italian Revenue Agency has clarified that a demerger followed by a transfer of shares in the demerging entity is not an abusive transaction, provided that (i) it ensures the continuation of the business activity of each participating company, and (ii) the companies involved pursue actual business activities and do not only contain cash, intangibles or real estate. This position is important because it marks a change of approach by the Revenue Agency. Under the former anti-avoidance rule, it used to take the position that demergers, especially when followed by a transfer of shares, were abusive.

5.3.2 Specific anti-avoidance rules

These rules, imposed by law, tax-authority practice and case law, include the:

- dormant companies rule
- rule on the tax residence of foreign companies and entities and foreign trusts
- CFC rule
- transfer pricing rule
- beneficial owner rule
- rule on the reclassification of shareholder loans
- hybrid mismatches rules.

Dormant companies rule

Italian companies, partnerships and permanent establishments of non-resident enterprises are treated as dormant if their taxable income falls below levels commensurate with the nature and book value of their assets – in other words, if they fail 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 rebut the minimum taxable income presumption by giving evidence of the circumstances that have prevented them from passing the vitality test. To this end, a company can either obtain a ruling from the Revenue Agency, confirming the circumstances, or give a separate indication of the 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 financial year if it has reported one of the following.

- (i) Tax losses for five consecutive financial years.
- (ii) Tax losses in four financial years and taxable income lower than the minimum deemed income of dormant companies in the fifth year.

Rule on the tax residence of foreign companies and entities and foreign trusts

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 real estate investment funds (REIFs), and (ii) it is directly or indirectly controlled by a resident company or individual.





Foreign trusts

Unless there is evidence to the contrary, foreign trusts are deemed to be Italian residents if both of the following apply.

- They are not established in a cooperative jurisdiction.
- 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 that is not a cooperative jurisdiction.

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 cooperative jurisdiction, 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 a cooperative jurisdiction, the current market value must be determined in agreement with the tax authorities, via the international ruling procedure²¹. If no agreement is reached or requested, 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.

As of 2018, resident companies which transfer their registered office to an EU/EEA cooperative jurisdiction are no longer allowed to defer the taxation of the deemed gains; the only option left is to pay the tax on the deemed gain in five annual instalments. However, any of the following events terminates the instalment regime.

- The company transfers its residence from a qualifying country to another jurisdiction that is not a qualifying country.
- The company is liquidated and wound 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.

Controlled foreign company rule (CFC rule)

Definition of a CFC

The 2019 Budget Law has significantly amended the CFC rule. According to the new provisions, a CFC is a foreign company in which (i) an Italian resident directly or indirectly, even through a trust company or other third party, holds the majority of votes or exercises a dominant influence or (ii) an Italian resident directly or indirectly has more than a 50 percent share in its profits, even through a trust company or other third-party company.

A company now qualifies as a low-taxed CFC if:

- it is subject to an effective tax rate that is lower than 50 percent of the effective burden that it would have incurred had it been an Italian resident, and
- more than one-third of its income is passive income, i.e. interest, dividends, royalties, capital gains on shares and revenues from financial leasing; revenues from insurance, banking and other financial activities; revenues from trading goods that are purchased from or sold to associated enterprises, with the addition of no or little economic value; revenues from supplies of services that are purchased from or provided to associated enterprises, with the addition of no or little economic value (whether the foreign entity sells goods or supplies services with little or no added value is determined on the basis of transfer pricing regulations).

²¹ See the section headed 'International ruling' in section 11.1.4. on p. 127.





Effects of the CFC rule

Under the CFC rule, the CFC's income is taxed to the shareholder resident in Italy. The income subject to tax in Italy is computed in accordance with the Italian rules and taxation is separate (e.g. tax loss carryforwards cannot be used to shelter the CFC income).

Safe-harbour rule

An exemption from the CFC rule is available to companies that can prove that an actual business is carried out in the foreign jurisdiction through local personnel, equipment, other assets and premises (the old rule also provided an alternative exemption based on proving an ultimate adequate level of taxation). The taxpayer can prove that it qualifies for the exemption by providing evidence in an application for a tax ruling or during a tax assessment.

Transfer pricing rule

This will be dealt with in section 6.

Beneficial owner rule

Certain domestic rules require the payee to be the beneficial owner of income in order to benefit from a WHT exemption or reduced rate (e.g. the measure implementing the Interest and Royalties Directive). Moreover, the Italian Revenue Agency often imposes this condition²². In practice, assessments of foreign entities, aimed at disallowing interest, royalties or even dividend exemptions are frequent.

Italian tax law does not contain a definition of beneficial owner. However, the Italian Revenue Agency has clarified that, in order to identify the beneficial owner of income, it may be necessary to look at the economic and contractual details of a transaction, consider whether the structure is appropriate, and even examine capability to manage financial risks²³.

In dealing with the application of DTT benefits, the Italian Revenue Agency has also clarified that an intermediary in charge of passing on income to other persons is not its beneficial owner. In such cases, the intermediary is not entitled to exploit the asset generating the income, and is prohibited from using the funds received on the current account for purposes other than passing on the income²⁴.

In other cases, the Revenue Agency requires the beneficiary to have an adequate structure, in terms of financial and management resources, and an adequate level of legal and economic substance. For instance, an entity with a light structure, no actual business and, de facto, no decision-making power, may be considered as a conduit company and not as the beneficial owner of interest.

The evaluation of beneficial ownership is particularly complex with respect to holding companies, whose activities generally do not require a significant physical presence.

Italian case law has basically confirmed this approach, highlighting that it is necessary to verify whether the recipient of the income has economic and legal autonomy in determining how to use the income. However, the Italian Supreme Court shows a more flexible approach to foreign pure holding companies that receive dividends.

Rule on the reclassification of shareholder loans

The Italian Revenue Agency has clarified²⁵ that foreign shareholder loans may sometimes be redefined as contributions of capital. If they are, the interest payments made by the Italian borrower cannot be deducted. This happens, for example, if "considering the borrower's financial situation, the investment should not have been made in that form" or if, in the contract, one or more of the following features point to a mismatch between the form of the debt and its substance.

²² See, for instance, the official forms for the WHT exemption/reduced WHT rate under the Interest and Royalties Directive, Parent-Subsidiary Directive, or DTT; Circular 32/2011, on the reduced 1.2 percent WHT rate on dividends paid to EU affiliates; Circular 6/2016 on interest payments in leveraged buyouts.

²³ See Circular 41/2011.

²⁴ See Resolutions 86/2006 and 167/2008.

²⁵ In section 3.3 of Circular 6/2016.





- The repayments of principal and payments of interest are deferred until those due to third-party lenders have been settled.
- The financial indicators defined in the financial covenants, which set out the terms of default, do not include, in the definitions of debt and interest, the shareholder loan and shareholder interest, respectively.
- The payments of interest and repayments of capital are subject to the same restrictions as dividends, capital reductions and reductions in capital reserves.

Hybrid mismatches rule

Starting from 2020 for calendar-year companies, a new set of provisions has been introduced (through the implementation of the ATA Directives²⁶ in Italy) targeting so-called hybrid mismatches. The new rules essentially deal with mismatches arising within the same group of companies (and related permanent establishments) and caused by (i) payments related to financial instruments, (ii) other types of payments, such as those related to intangible assets, and (iii) hybrid entities. In brief, hybrid mismatches arise in the following circumstances:

- An entity makes a payment, bears an expense or realises a tax loss.
- That entity is linked to another, which is tax-resident in a different country (in the case of a payment, the second entity does not necessarily need to qualify as the recipient of the payment).
- At least one entity is subject to corporate tax in an EU Member State.
- The tax laws of the two countries adopt a different definition and tax treatment for (a) the legal instrument or relationship by which the payment is made, the expense is borne or the tax loss is realised, or (b) the entity that makes the payment, or (c) the entity that receives the payment.

As a result of the legal mismatch, the following tax situations may arise.

- The same payment may be deducted in both countries (double deduction).
- The payment may be deducted in the country of the payer but not included in the tax base in the country of the recipient (deduction and non-inclusion).
- The payment may be tax-exempt in one country but not included in the tax base in the other country (non-taxation and non-inclusion).

Briefly, the new hybrid mismatch rules establish the following.

- If the Italian entity is the recipient and the payment is deducted by the paying entity, deduction is not allowed.
- If the Italian entity is the payer, the deduction is not allowed unless the tax inclusion of the payment in the other jurisdiction is proved.

The new rules targeting hybrid mismatches are very complex, as they also target particular situations such as imported mismatches, reverse hybrids and dual-residence mismatches. MNE groups operating in the EU should pay careful attention to their existing tax optimisation structures in order to comply with the new requirements.

²⁶ EU Anti-Tax Avoidance Directives no. 1164/2016 (ATAD) and no. 952/2017 (ATAD 2).







6. Transfer Pricing

6.1 General principles

Italian transfer pricing regulations directly refer to the arm's length principle stated in the OECD Transfer Pricing Guidelines.

The principle that international transactions between related parties must be in compliance with the arm's length standard means that, in determining the value of components of income derived from intragroup transactions, it is necessary to take into account the conditions and prices that would have been agreed between independent parties, operating at arm's length conditions in comparable circumstances.

The arm's length test is based on the methods identified by the 2017 OECD Transfer Pricing Guidelines. In their official instructions, the Italian tax authorities still recommend that the Comparable Uncontrolled Price (CUP) Method be applied whenever possible. In practice, the principle established by the OECD Transfer Pricing Guidelines – that the method most suited to the circumstances of the case must be selected – is commonly accepted and applied.

The application of the arm's length principle may trigger both increases and reductions in taxable income. However, reductions are only accepted in the following cases.

- Under agreements reached by the competent tax authorities in the context of a MAP.
- After audits carried out as part of international cooperation activities, the results of which are shared by the cooperating countries.
- Upon request by the taxpayer, following a final upward adjustment of the taxable income by a country with which Italy has a tax treaty allowing an adequate exchange of information (i.e. unilateral corresponding adjustments – a procedure that can now be concluded within 180 days).

Transfer pricing regulations in Italy only apply to cross-border transactions between related entities (i.e. an Italian company and its direct or indirect parent, subsidiary or sister companies). The application of transfer pricing rules to domestic transactions is excluded by law and this principle has been upheld in several Italian court cases.

Transfer pricing rules apply for both IRES and IRAP purposes. A Revenue Agency tax ruling has recently clarified that, in certain circumstances, transfer pricing adjustments fall outside the scope of VAT.

6.2 Documentation issues

In drawing up transfer pricing documentation, reference is generally made to (i) the principles established in the OECD Transfer Pricing Guidelines, supplemented 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. Penalty protection is subject to certain requirements: (i) that the taxpayer prepares in advance and discloses the existence of transfer pricing documentation in its annual tax return; (ii) that, on request, the taxpayer submits the documentation in a timely manner; (iii) that the documents strictly comply with the template indicated in the tax authorities' guidelines; (iv) that the transfer pricing documentation is deemed to be appropriate by the Italian tax authorities in their tax audit report, i.e. when the documentation provides the tax inspectors with the information necessary to satisfactorily analyse transfer prices.





If the taxpayer is in possession of proper transfer pricing documentation, the burden of proof generally lies with the tax authorities; vice versa, 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.

Italian transfer pricing regulations provide templates for a master file/country-specific documentation; however, the indications given in OECD BEPS Action 13 and the revised Chapter V of the 2017 OECD Transfer Pricing Guidelines, with reference to the master file/local file approach, have not yet been implemented in Italy.

For certain transactions, such as intra-group services, general Italian CIT rules require evidence that (i) the services are actually related to the business, and (ii) the company receiving the services obtains or can reasonably expect to obtain a benefit from them, in view of its ordinary business activity. This circumstance must be demonstrated by appropriate (additional) documentation, which must be shown to the Italian tax inspectors in the event of a tax audit. The Italian tax authorities generally take a very aggressive approach to Italian companies that are members of multinational groups and that deduct intra-group charges for services, usually disallowing the deduction if the charges are not appropriately documented.

6.2.1 Country-by-Country (CbC) reporting

There are now CbC reporting obligations - pursuant to OECD BEPS Action 13 - for Italian parent companies of groups with consolidated turnover of over EUR 750 million. The obligation also extends to Italian subsidiaries when the ultimate parent company has to prepare consolidated financial statements but is resident in a country that has not implemented CbC reporting rules or does not exchange information gathered under the CbC reporting rules.

The CbC report must be submitted within 12 months of the last day of the MNE group's financial year.

The content of the CbC report, the first year for CbC reporting, the CbC reporting dates, and the submission procedures are all laid down in rules and guidelines.

Failure to comply with the CbC reporting obligation triggers an administrative penalty ranging from EUR 10,000 to EUR 50,000.

6.3 Penalties

In the event of a tax assessment, no penalties should apply if the taxpayer qualifies for the penalty-protection regime described above. Otherwise, standard CIT penalties 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 an early settlement.

In certain circumstances, criminal penalties may also apply.

6.4 Advance tax agreements for enterprises with international activities

Advance tax agreements for enterprises with international activities resolve both transfer pricing and other international taxation matters. With specific reference to transfer pricing, unilateral, bilateral and multilateral APAs have been introduced in Italy, to define in advance the methods to be used in calculating the arm's length value of transactions subject to transfer pricing regulations. The APA procedure may also be used to determine the attribution of profits between a permanent establishment and its head office





and to ascertain in advance whether a foreign enterprise has a permanent establishment in Italy.

The APA procedure is reserved for enterprises with international activities, namely:

- resident companies that meet the conditions imposed by 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, which must be accompanied by full documentary evidence that the applicant is eligible for the procedure. The APA 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 has been obtained.

The procedure ends with the taxpayer and the director of the APA Office signing an agreement that is binding on the taxpayer and the Italian tax authorities for the financial year in which the agreement is issued, and for the following four years, provided the factual and legal circumstances remain unchanged.

An APA agreement may also apply retroactively in two situations. First, if the APA is based on a MAP, under a DTT, it is binding back to the financial year in which the APA application was submitted. Second, if the factual and legal circumstances on which the APA is based were the same in prior financial years, the taxpayer may roll back the terms of the APA to the financial year in which the APA application was submitted, and amend its tax returns, without facing any penalties.

If an APA is not reached, a written report is drawn up.

Over the five financial years in which the APA is valid, the tax authorities may only carry out tax assessments in relation to matters other than those covered by the APA. After the APA has been signed, the APA Office may conduct audits in order to assess whether the terms and conditions are being respected and whether there have been any changes in the factual or legal circumstances on which the APA is based. The taxpayer must submit, periodically or on request, any documents or information that enable the APA Office to monitor the company's compliance with the terms and conditions of the APA. The APA Office can also visit the premises of the company, at a time agreed beforehand; the APA Office's activities must be described in a report, a copy of which is given to the company's legal representative.

If the company violates the APA, in whole or in part – i.e. the APA Office realizes, from documentation, information, visits to the company's premises or other sources, that the company has not respected the terms of the agreement or demonstrates a lack of cooperation or transparency – the APA Office will serve the company a notice inviting it to submit its arguments of defence within 30 days. If the company fails to submit its arguments on time, or if the APA Office believes that the company's arguments do not sufficiently disprove the accusations against it, the APA Office will notify the company that the agreement is invalid.

Italian regulations also explain how the APA can be amended if the original circumstances change, and how the APA can be renewed. Up to 90 days before it expires, taxpayers can submit an application to renew the APA. Amendments and renewals may both involve an inquiry or further debate between the APA 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.

7.1.2 Tax residents of Italy

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 financial year (i.e. for 183 days or more in a calendar year).

- The individual is registered in the *Anagrafe* (the Office of Records of the Resident Population in Italy).
- 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 minors and on half the income generated by (i) jointly-owned marital assets and (ii) family assets.

7.1.3 Non-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

can benefit from all allowances that resident individuals are entitled to, while still qualifying (and being taxed) as non-resident individuals, on condition that they do not benefit from similar allowances in their state of residence.

This 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 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 IRPEF. In addition, regional and municipal taxes are levied; these vary according to the place of residence and the regulations issued by the regional and municipal authorities.

Individuals who are resident in Italy are subject to wealth taxes (IVIE and IVAFE) on real estate and financial products held outside Italy.

7.2 Taxable income

7.2.1 Categories

Resident individuals are subject to IRPEF on the following worldwide income:

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

The aggregate taxable income is calculated by adding together the income of each category; only losses arising from a business, trade 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 financial year in connection with employment. All types of pensions and equivalent allowances are deemed to be income from employment.

No deductions from employment income are allowed for work-related expenses.

As a general rule, all reimbursements by the employer are taxable to 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 financial 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. 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 complementary pension funds, the tax treatment differs considerably.

- Periodical payments made by pension funds (including those derived from TFR payments and tax-deductible employee contributions) are subject to separate taxation at a maximum flat rate of 15 percent, varying in accordance with the years accrued.
- 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 bonds or government bonds of cooperative jurisdictions, the substitute tax is 20 percent but the taxable 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).

Remuneration paid to the members of a board of directors or supervisory board who are not tax residents of Italy is subject to a final WHT of 30 percent.

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 IRPEF. 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. The partners of a partnership engaging in trade may opt to have partnership income taxed at the corporate tax rate of 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 financial year (in cash or in kind, including profit shares) and the expenses incurred in practising 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 are 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.

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, by both the employer and 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.

Reimbursements for the following are not included in taxable income:

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

If a company car or motorcycle is made available to an employee, the taxable benefit is 30 percent of the amount calculated on the basis of published tables and an assumed annual mileage of 15,000 km.

If an employee receives a low-interest loan from an employer or a third-party lender, the taxable benefit is 50 percent of the difference between 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's income 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.

Starting from 1 January 2019, the threshold will increase to EUR 4,000 for children up to the age of 24 years.

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.



The same deductions apply to same-sex couples who have entered into a civil union.

Dependent children – EUR 1,220 (for children up to three years) and EUR 950 (for children over three years) for dependent children, 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;
- two children, the deduction is not available for income of over EUR 110,000;
- three children, the deduction is not available for income of over EUR 125,000;
- four children, the deduction is not available for income of over EUR 140,000, 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, 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 amount of income. 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:

- the portion of medical expenses exceeding EUR 129.11, incurred by the taxpayer, his/her spouse or other dependents, and including fees charged by specialists;
- veterinary expenses: up to EUR 387.34;
- voluntary life insurance premiums and accident premiums not exceeding EUR 530 (provided that certain conditions are met);
- insurance premiums covering assistance for disabled persons: up to EUR 750;
- insurance premiums covering the risk of no longer being able to complete ordinary daily tasks: up to EUR 1,291.14;
- insurance premiums covering the risk of calamities affecting housing;
- interest paid to banks resident in the EU on mortgage loans (for owner-occupied dwellings) secured by property in Italy, up to a maximum of EUR 4,000 per year (if other taxpayers share ownership of the property the deduction is calculated in proportion to the 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;
- nursery school tuition: up to EUR 632;
- elementary, junior and high-school tuition: up to EUR 786;
- university fees up to the amount of tuition fees payable to state schools and universities;
- expenses for children's sports (for children aged 5 - 18 years old): up to EUR 210 per child;



- expenses paid to real estate agents, up to a maximum of EUR 1,000;
- grants for particular public objectives;
- season tickets for public transport services, up to a maximum of EUR 250 (including costs incurred for family members);
- expenses incurred to help individuals with a specific learning disability, until the completion of secondary school;
- rents of university students 'away from home', up to a maximum amount of EUR 2,633.

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 (50 percent);
- energy retrofits (65 percent);
- earthquake-proof building renovations (from 70 to 85 percent);
- maintenance of gardens and terraces (36 percent – with a cap of EUR 5,000 on expenses).

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 2018. The deduction for building renovation and energy retrofits must be spread over 10 years.

7.4 Tax rates

7.4.1 General rules

The following rates of IRPEF apply.

TAXABLE INCOME	TOTAL TAX ON INCOME 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 are 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.

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 shareholding	Qualifying shareholding
Private individual (dividend taxed as income from capital).	26 percent final WHT on 100 percent of the dividend.	26 percent final WHT on 100 percent of the dividend.

There is a temporary regulation for the distribution of dividends from qualifying shares, approved between 1 January 2018 and 31 December 2022 and constituted by profits produced by 31 December 2017. In such cases the dividends are taxed according to the previous rules (therefore, with the progressive IRPEF rates on a tax base reduced to 40 percent, 49.72 percent or 58.14 percent, depending on the year in which the profits were produced).

Foreign dividends

Recipient	Non-qualifying shareholding	Qualifying shareholding
Private individual (dividend taxed as income from capital).	26 percent final tax on the dividend net of the tax paid in the foreign country.	26 percent final tax on the dividend if it derives from a company located in a cooperative jurisdiction. (Progressive taxation on 100 percent of the dividend if the shareholding is in a company in a low-tax jurisdiction. The tax basis is reduced to 50 percent of the dividend if it is proved that the foreign company carries on an effective activity in the low-tax jurisdiction).

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 (from 1 January 2019 the tax rate will be 26 percent).

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, whether Italian or foreign (provided that the foreign entities are in a cooperative jurisdiction), is subject to a final WHT 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 WHT of 26 percent. Interest on bank and postal current accounts is subject to a final WHT of 26 percent. Taxpayers may choose to tax interest at progressive tax rates.

Royalties

Royalty income includes that derived from the third-party use of IP (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 certain 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 landlord 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 tax base is 100 percent of the rental income stipulated in 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 are 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, subject to the DTT provisions.

Taxation of investment capital gains

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

The tax rate is 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 WHT, 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 financial 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 return²⁷ must be filed by **23 July** of the subsequent year, whereas the filing deadline for the *Redditi PF* return is **30 September**.

The deadlines may be extended further by the Italian government.

7.5.3 Foreign asset monitoring

Regardless of their obligation to file a *Redditi PF* return, all individuals who are tax residents of Italy must comply with exchange control regulations in Italy and declare their foreign investments.

Tax residents are required to report all assets held outside Italy on the RW Form, which is filed as part of the *Redditi PF* return. 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 WHT and other tax credits. It is possible to pay by 31 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 WHT 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 2019 as an example):

- Payment by 31 July 2019 – interest of 0.4 percent.
- Payment between 31 July and 30 August 2019 – if the payment is made between 1 and 15 August 2019, there is a reduced penalty equal to 0.1 percent of the unpaid tax for each day of delayed payment, up to and including the payment date, plus interest. Between 16 and 30 August 2019, the penalty is 1.5 percent of the unpaid tax, plus interest.
- Payment between 31 August 2019 and 29 October 2019 – 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 than assessed or higher credits/deductions than assessed) are subject to penalties of between 90 percent and 180 percent of the additional tax due. In some circumstances, criminal penalties may be imposed.

²⁷ The income tax return that must be completed by individuals who are employees, pensioners, members of co-operatives and taxpayers with fixed-term contracts.





7.6 Other taxes

7.6.1 Wealth tax on foreign assets

Foreign financial products held outside Italy are subject to IVAFE. For bank accounts, postal accounts and savings accounts, the tax is fixed at EUR 34.20 per account, if the annual average balance is higher than EUR 5,000. Other foreign financial products are subject to a tax rate of 0.2 percent of the value at the end of the financial 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. The tax amounts to 0.76 percent of the purchase price or, in some cases, of the foreign cadastral income, in proportion to the percentage of ownership and days of possession. If the property in question is used as the principal residence then the tax rate is reduced to 0.4 percent.

7.6.2 Municipal property tax (IMU)

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

The tax 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 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.

- Four percent for beneficiaries directly related to the donor or the testator (i.e. spouse and children). An exemption is given for the first EUR 1 million of assets and cash transferred to each beneficiary (the threshold rises to EUR 1,500,000 for disabled beneficiaries).
- Six percent for siblings of the donor or the testator. An exemption is given for the first EUR 100,000 of assets and cash transferred to each beneficiary.
- Six percent for other relatives, with no tax exemptions.
- Eight percent for beneficiaries not related to the donor or the testator, 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.



7.7 International aspects

7.7.1 Expatriates

Income derived by resident employees from an activity permanently performed abroad is taxable on the basis of notional salaries determined annually by decree of the Ministry of Employment and Social Security. This applies only if (i) the activity performed abroad is the exclusive object of the employment, (ii) the activity is not occasional, and (iii) the employee stays abroad for more than 183 days of the year.

The 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 WHT 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 IRPEF 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 on a per-country basis.

The credit must be claimed, upon penalty of forfeiture, in the tax return for the financial 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 to 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 IRPEF on Italian 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 WHT 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 non-residents.

Investment income and professional income are subject to a final WHT or substitute tax. Where WHT 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 WHT 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 or practised in Italy through a permanent establishment or a fixed base for at least three months.

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

In general, interest payments to non-resident individuals are subject to a final WHT 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 that is outside the European Union and has 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 and 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 WHT, 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 IRPEF 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 DTT applies.

7.7.4 Special flat-tax regime for new residents

High net worth individuals who become new residents of Italy may opt for a favourable tax regime, allowing them 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 - see 7.5.3) and related wealth tax payments.

Ordinary taxes will only be applied to:

- capital gains from qualifying shareholdings, realised in the first five financial years;
- Italian income.

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





The regime has been available since FY 2017 and, once opted for, runs 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 as the applicant must:

- have been tax resident outside Italy for at least nine of the 10 previous financial years;
- become a resident of Italy under Italian tax law;
- opt for this regime through the Italian annual *Redditi PF* return.

The applicant can apply for a tax ruling from the Italian tax authorities in order to ensure that the requirements are satisfied. The tax ruling application can be submitted even before the individual moves to Italy.

7.7.5 Special tax regime for certain inbound workers

The Italian government offers a tax break to certain workers who move to Italy, by treating 50 percent of their employment or self-employment income as exempt from IRPEF. The exemption runs for five financial 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 financial years preceding their transfer;
- b) who remain resident in Italy for at least two financial years;
- c) who work for an Italian company and have an employment contract with an Italian company, a company that controls an Italian

company, or a company directly or indirectly controlled by an Italian company;

- d) whose work is carried out mainly in Italy;
- e) who occupy managerial or executive roles or are highly qualified/specialised employees.

The same regime is also available for graduates (EU citizens and citizens of non-EU countries with which Italy has a DTT or an information exchange agreement) who have:

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







8. Employment law and immigration

8.1 Employment law

8.1.1 Conditions of employment

National collective bargaining agreements (CCNLs²⁸)

CCNLs between employer associations and trade unions broadly govern employment relationships and the resulting rights and obligations.

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; in general, 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, called '*superminimi*', on top of the minimum basic salary.

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

Employers are not required to justify the use of fixed-term employment contracts that are not longer than 12 months. For any further period, or for contracts longer than 12 months, fixed-term employment contracts are allowed only when there are exceptional and temporary business needs.

²⁸ In Italy a national collective bargaining agreement is called a '*contratto collettivo nazionale di lavoro (CCNL)*'.





The maximum duration of a fixed-term contract is 24 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. In any event, employees on fixed-term employment contracts and temporarily supplied employees (see below), counted together, cannot exceed 30 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), but normally the overtime rate is established by the applicable CCNL.

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. 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.

Maternity leave

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

Italian employment 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 to INPS, together with a medical certificate stating that this arrangement will not harm the mother or the child.

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

Optional maternity leave can be taken in addition to compulsory leave.

Italian employment 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 if:

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

End-of-service allowance (TFR - *Trattamento di fine rapporto*)

Regardless of the circumstances under which their employment relationship ends, employees are entitled to receive TFR, which is approximately equal to one month of 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, employees may ask their employer to pay the TFR into a pension fund.

Types of employment contract

Open-ended contracts

The standard type of employment contract is the open-ended one.

Fixed-term employment contracts are allowed, but subject to specific restrictions (see above).

Apprenticeship contracts

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

The contract must be drawn up in writing and contains 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 percent of their apprentices in the 36 months prior to the new intake.

On-call contracts

These contracts are allowed for employees under 24 or over 55 years old.

In any three-year period, the number of days worked by an employee for an employer cannot exceed 400 (except in the tourism, entertainment, and commercial business sectors).

Freelance agreements

Coordinated and continuous freelance agreements are automatically reclassified as employment agreements if the services are personally rendered by the consultant and if the consultant is bound by working-time and workplace directives. Exceptions are provided for certain categories of workers, such as those identified by CCNLs, individuals enrolled in professional registers (e.g. lawyers, engineers, architects), members of governing and supervisory boards, contractors providing services to sports associations, and companies affiliated with national sports federations.

Staff-leasing and temporary supply of manpower

Companies can use agencies, duly authorised by the Ministry of Employment, to procure workers on a permanent or temporary basis. When workers are supplied on a permanent basis, this is known as staff-leasing.

Staff-leasing can be used in any sector. However, the number of workers used under staff-leasing arrangements cannot exceed 20 percent of the open-ended employment contracts in force on 1 January of the same year (or the limit established by the applicable CCNL).





Temporarily supplied employees and employees on fixed-term employment contracts (see above), counted together, cannot exceed 30 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.

8.1.2 Termination of individual and collective employment contracts

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 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.).

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 received by the employee will depend on the size of the employer, the concrete situation and whether the employee was hired before or after the Jobs Act came into force.

In all contracts signed after the entry 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, for which compensation 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

CCNLs for executives (which are different for each sector) generally state that there must be 'good grounds' for their dismissal. Therefore, an executive may contest dismissal and seek damages if the dismissal is not supported by any valid reason.

Notice period. CCNLs for executives specify the length of the notice period, which depends on the executive's length of service.

Redundancy procedures - collective dismissals

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

When a company intends to make a collective dismissal, it must follow a special redundancy procedure. This procedure also applies when a company is closed down.

The steps to be taken are established by law.

- 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 Employment (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 they receive 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 Employment. This phase involving the Ministry of Employment ends 30 days after the date of the notice sent by the company to the office to inform 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 anyway, even without reaching an agreement, 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 usually sign an official settlement agreement at the local office of the Ministry of Employment 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 Rules on the posting of workers to Italy

Italy has implemented Directive 2014/67/EU concerning the posting of workers in the EU. The following main rules apply.

- When workers are posted to Italy, foreign employers and placement agencies must give **notice** to Italy's Ministry of Employment at least 24 hours in advance, and meet any mandatory obligations imposed by Italian immigration law.
- The home company must appoint someone in Italy to keep the secondment documentation (employment contract, pay-slips, etc., all of which must **be translated into Italian**) and someone to liaise with the trade unions.
- The national employment inspection bodies will verify the **authenticity of the secondment** by checking 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. In this case, both the home and host company will be subject to sanctions.
- Workers seconded to Italy must be granted the **same treatment** (both economic and regulatory) as workers of the same level hired in Italy and performing the same duties.
- 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 INAIL²⁹, 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 early-retirement 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 approximately 67 years old (men and women). This age will rise in years to come, also taking into account increasing life expectancy.

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

Early-retirement pensions

Employees registered with INPS are entitled to an early-retirement pension when they meet one of the following requirements.

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

This requirement will increase gradually, up to 45 years of contributions.

For the period 2019-2021 the Italian government has established - on a trial basis - a new pension option called '*quota 100*'. This applies to everyone who, on 31 December 2018, had at least 38 years of contributions and was 62 years old.

8.2 Immigration

8.2.1 EU citizens

Entry requirements, immigration procedures and occupational 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 valid passport/ID card can travel in Italy and are exempt from entry/visa requirements.

Residence

EU citizens who reside in Italy for fewer than 90 days do not have to register at the town hall. If

²⁹ Istituto Nazionale per l'Assicurazione contro gli Infortuni sul Lavoro - National Institute for Accidents at Work.





an individual remains in Italy for more than three months, registration is necessary.

Employment

EU citizens are free to work in Italy without 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 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.

A 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 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

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 the local branch of the Immigration Office (*Prefettura Sportello Unico per l'Immigrazione*). The Immigration Office checks the terms of employment and the documentation required and then issues the work visa, along with a *Nulla Osta* clearance certificate. The terms of employment cannot be less favourable than those established by the relevant CCNL.

Once the *Nulla Osta* clearance certificate has been obtained, a visa must also be obtained from the Italian diplomatic mission of the foreign worker's 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 arrival. Within this same period, the worker and the Italian employer must sign a 'stay contract' summarising the main terms of employment.

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 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 transfer of ownership clause, 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.

VAT is also due on all imports.

For VAT purposes, the financial year is the calendar year.

9.2 Rates

The standard rate of VAT is 22 percent but there are reduced rates of VAT for certain goods and services, as well as zero rates and exemptions for others.

10 percent VAT rate

- Certain foods
- Domestic fuel and power
- Public transport
- Certain pharmaceutical products
- Water
- Hotel accommodation
- Services of writers and composers
- Social housing
- Renewable energy
- Etc.

5 percent VAT rate

- Services provided by cooperative companies and their consortia: medical, social-care, educational, home-care, outpatient, community services and the like
- Authorised water passenger transport services operating in urban areas
- Etc.

4 percent VAT rate

- Basic foodstuffs
- Books, newspapers and e-books
- A person's main dwelling
- Certain pharmaceutical products
- Medical equipment and aids for the disabled
- Etc.

Zero-rated supplies

- Exports and EU supplies
- 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
- Etc.





Exempted supplies

- Financial services
- Insurance services
- Tax-collection services
- Lotteries, betting, and other games of chance
- Certain transactions involving residential property
- Postal services
- Cultural services
- Certain real-estate transactions.
- Etc.

NB. It is not possible to recover VAT on exempt supplies.

The 2019 Budget Law provides for a gradual increase in VAT rates from 1 January 2020.

- The reduced 10 percent VAT rate will increase to:
 - 13 percent on 1 January 2020.
- The standard 22 percent VAT rate will increase to:
 - 25.2 percent on 1 January 2020
 - 26.5 percent on 1 January 2021.

The 'super' reduced VAT rate of 4 percent will remain unchanged.

These VAT rate increases will not apply if certain budgetary targets are met.

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.

The direct identification form and instructions, as well as the form and instructions for appointing a VAT representative, can be found on the Italian Revenue Agency's website:

www.agenziaentrate.gov.it

The penalty for failing to register for VAT on time ranges from EUR 500 to EUR 2,000.

Certain simplification schemes may apply as follows.

9.3 Registration

9.3.1 Italian entities

If a business makes taxable supplies in Italy, it is required to register 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 which make taxable supplies in Italy that are not subject to the reverse charge mechanism.

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, the transaction qualifies as a domestic supply (i.e. not as a cross-border transaction) and its business customer must account for acquisition tax in Italy. 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 must be shifted to the customer if (i) the customer is established in Italy and registered there for Italian VAT purposes, and (ii) the supplier is a non-established entity. This rule is applied, for example, in the following cases.

- Customers established and VAT-registered in Italy are liable to account for Italian VAT under the compulsory reverse charge mechanism when domestic supplies of goods and services are made by **suppliers established in other Member States**; for this purpose, customers must complete the invoices issued by their suppliers by adding, amongst other details, the Italian VAT rate and the amount of Italian VAT to be paid.
- For domestic supplies of goods and services made by **non-EU suppliers**, Italian customers must issue a self-billed invoice, charging Italian VAT to themselves.

9.4 VAT grouping

9.4.1 VAT grouping rules

Since 1 January 2018 taxpayers have been able to opt for VAT grouping (with the VAT group becoming effective from 1 January 2019 at the earliest). VAT group members must be taxable persons (not necessarily companies) established in Italy. Permanent establishments or head offices of Italian permanent establishments located abroad are not eligible to join. A VAT group can be set up between Italian subsidiaries of a foreign entity, as long as the foreign entity is based in a country (EU or non-EU) that has an exchange of information agreement with Italy. Companies that are in the process of being wound up or that are subject to bankruptcy or asset-seizure procedures through the courts are also excluded.

To form a VAT group, taxable persons must have financial, economic and organisational links. Therefore, passive holding companies, whose sole activity is the ownership of shares, are ineligible to join. Mixed holding companies, which not only own shares but provide additional services to their subsidiaries, can instead join the VAT group.

- The financial link is based on control, and must have existed since 1 July of the calendar year preceding that in which the VAT group becomes effective. The person exercising 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 main business purpose of the companies, as emerging from their deed of incorporation, must be taken into account, whilst the ATECO code is irrelevant.
- The organisational link is based on legal coordination between the decision-makers.





It is presumed that if a financial link exists between potential members of a VAT group, the economic and organisational links are also present. However, that presumption can be rebutted before the Revenue Agency, i.e. it is possible to argue that economic and organisational links do not exist.

A group is set up by all the taxable persons who are established in Italy and have the necessary links (the 'all-in, all-out principle'). The representative of the group must exercise the option to form the VAT group by filing a statement containing all the relevant information, such as details of the members of the group, confirmation of the links between them, and the activities 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. Therefore, an option exercised in October 2019 would lead to the group being effective only from January 2021, whereas an option exercised on 30 September 2019 would lead to the group becoming effective in January 2020. New members can join once they meet the necessary conditions.

Form AGI/1 has to be used when opting for the application of the VAT grouping regime.

If a taxable person meets the conditions to be part of the VAT group but is not mentioned in the option, the VAT group ceases to exist the year after that in which the irregularity is ascertained, unless that person exercises 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. The timing of the revocation determines the date on which the group is dissolved. Any member that ceases to have the necessary links, or to meet the other necessary conditions, ceases to be a member.

The member representing the group is the parent company or, if the parent company is established outside Italy, the VAT group member with the highest turnover or revenue.

The representative has the most responsibility for ensuring compliance (such as filing the annual VAT return, reporting periodical VAT settlements, and paying the output VAT on a periodical basis), but all the members are jointly and severally liable for VAT debts. Other obligations, such as e-invoicing and VAT bookkeeping, can be discharged centrally by the representative or separately by each of the members.

The group's internal transactions are disregarded for VAT purposes while supplies by a member of the group to a third party or by a third party to a member of the group are treated as supplies carried out by or to the VAT group. Moreover, the principles set out by the ECJ in the Skandia Case³⁰ have been implemented in Italy, with effect from 1 January 2018 (no retroactive application). Therefore, head office to branch charges are no longer disregarded for VAT purposes when the head office or the branch belongs to a VAT group in Italy or another jurisdiction. This means that goods and services provided:

- by a head office (or branch) established in Italy and belonging to an Italian VAT group, to a branch (or head office) established in another state, are deemed to be supplied by the VAT group to a separate taxable person;
- by a head office (or branch) established in another state, to a branch (or head office) belonging to an Italian VAT group, are deemed to be supplied by a separate taxable person to the Italian VAT group;
- by a head office (or branch) established in another state and belonging to a foreign VAT group, to a branch (or head office) established in Italy, are deemed to be supplied by the foreign VAT group to a separate Italian taxable person;
- by a head office (or branch) established in Italy to a branch (or head office) established in another state and belonging to a foreign VAT group, are deemed to be made by a separate Italian taxable person to the foreign VAT group.

³⁰ *European Court of Justice Case C-7/13, in which the court ruled on the VAT treatment of transactions between a head office and its branch when a legal entity is part of a VAT group (judgment of 17 September 2014).*





The new rules apply to transactions dating from 1 January 2018, although the VAT grouping rules will actually be effective in Italy only from 1 January 2019.

The special simplified compliance obligations for banks, insurance companies and fund managers apply even when they belong to a VAT group.

9.4.2 Consolidated VAT regime

As an alternative to the VAT group regime, the consolidated VAT regime³¹ remains in force. Under this regime, members may pool their VAT positions to offset their respective VAT debts and credits, even if each group member has its own VAT number. When this happens, intra-group 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 join the group cannot be used to offset the net VAT payment positions of other members.

The option for the consolidated VAT regime should be exercised in section VG of the annual VAT return submitted during the financial year in which the consolidated VAT regime starts (e.g. the option for VAT consolidation from 2019 is exercised in the annual VAT return for FY 2018, to be submitted by the end of April 2019). Once elected, the regime remains in place until revoked.

The minimum holding period for this regime should be observed from 1 July of the calendar year preceding that in which the option is exercised.

9.5 Returns

9.5.1 Annual returns

All registered businesses are required to submit VAT returns annually. Annual VAT returns for FY 2017 onwards must be filed between 1 February and 30 April of the following year. 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.

VAT is paid on a monthly or quarterly basis and repayments are made on an annual basis (quarterly repayment claims are admitted only in certain cases).

9.5.2 Guarantees

Taxpayers who submit guarantees in order to obtain VAT refunds are entitled to receive a lump-sum indemnity corresponding to 0.15 percent of the guaranteed amount, for each year of the guarantee. The purpose of this rule is to enable taxpayers to recover part of the costs of the guarantee. This indemnity is paid on expiry of the statute of limitations for the year to which the refund claim refers or, if a tax assessment notice has been served, when the right to obtain the VAT refund has been finally certified by the Italian Revenue Agency. The rule applies to VAT refunds claimed in annual VAT returns from FY 2017, and to the quarterly VAT refund claim filed for the first quarter of 2018. In practice, the first indemnities will become due in 2023 (when the statute of limitations for FY 2017 expires).

9.5.3 VAT invoice reporting

Since 2017, VAT reporting obligations have included (i) the quarterly reporting of details of invoices received and issued (so-called '*Spesometro*'), and (ii) the quarterly reporting of periodical VAT settlements. Both of these are due by the end of the second month following the relevant quarter.

³¹ Governed by article 73 of the Italian VAT Act.





However, the “*Spesometro*” could be submitted on a six-monthly basis for FY 2018 and will no longer be required from 1 January 2019.

From 1 January 2019, Italian taxpayers will have to report the invoice details of cross-border transactions by the end of the month following that in which the invoices are issued or received (other than those transmitted through the SDI - see section 9.8.3 below - and those for imports documented by customs bills).

A penalty of EUR 2 per invoice (capped at EUR 1,000 per quarter) may apply for failing to submit a report or submitting an incorrect one. However, if the submission is made or amended within 15 days of the deadline, penalties will be reduced by 50 percent and capped at EUR 500.

9.5.4 Intrastat

In Italy, European sales listings and statistical report forms (Intrastat) have been combined. They are normally referred to collectively as Intrastat returns. There is one return for outbound supplies of goods and another return for outbound supplies of services. The Intrastat returns for inbound supplies - one for goods and one for services - are no longer due for tax purposes, but are required for statistical purposes.

Intrastat returns may be submitted on a monthly or quarterly basis, depending on levels of EU transactions over the previous four quarters.

Monthly returns for intra-EU **sales** of goods and services should be submitted when these transactions are equal to or higher than EUR 50,000 in at least one of the four previous quarters. However, the statistical section of the monthly Intrastat return for intra-EU sales must be filled in only if the sales are equal to or higher than EUR 100,000 in one of the previous four quarters.

Monthly returns for intra-EU **purchases** of goods and services should be submitted, for statistical purposes, when these transactions are equal to or higher than EUR 200,000 for goods and EUR 100,000 for services in at least one of the four previous quarters.

Failure to submit Intrastat returns on time may result in a penalty ranging from EUR 500 to EUR 1,000, plus an additional penalty for statistical violations, ranging from EUR 500 to EUR 5,000.

The Intrastat forms can be found on the following website:

www.adm.gov.it

9.6 VAT recovery

In general, input VAT incurred by taxpayers to purchase goods and services used within their business activity is recoverable.

9.6.1 Time limit for VAT recovery

After a change of rules in 2017, there is less time to recover input VAT. Under the previous rules, input VAT could be recovered, at the latest, through the annual VAT return for the second year after that in which the VAT became payable (i.e. when the tax point was triggered). Now, input VAT incurred on purchase invoices and customs bills issued from 1 January 2017 can be recovered, at the latest, by the deadline for submission of the annual VAT return for the year in which the VAT becomes payable, i.e. when the tax point is triggered.

However, the Italian Revenue Agency has provided guidance on this matter and – surprisingly – has taken a very favourable position towards VAT payers. It has clarified, among other things, how to identify the final deadline by which the VAT recovery right can be exercised (intra-EU purchase invoices are not substantially affected by these changes in the law).

The Revenue Agency recognises the principles stated by ECJ case law and in particular in Case C-152/04, according to which: “*the right to deduct must be exercised in respect of the tax period in which the two conditions required by that provision are satisfied, namely that the goods have been delivered or the services performed and that the taxable person holds the invoice or the document*”





which, under the criteria determined by the Member State in question, may be considered to serve as an invoice". Based on this, the Revenue Agency clarifies that the VAT recovery right is triggered in the calendar year when the following two conditions are both met.

- The tax point is triggered/the VAT becomes chargeable.
- The customer receives a valid VAT invoice.

Therefore, the right to recover VAT can be exercised "at the latest in the annual VAT return for the year in which both the above conditions are met and with reference to that year".

In October 2018 there was a slight modification to the time limit for input VAT recovery, enabling VAT payers to recover the input VAT in the VAT settlement for the month when the tax point is triggered, even if the purchase invoice is received and recorded in the input VAT ledger by the 15th of the following month. This rule does not apply to transactions whose tax point arises in a financial year different from that in which the purchase invoice is received.

Essentially, for purchase invoices/customs bills dated 2018 and received in 2019, the following situations could arise.

- The invoices/customs bills are posted in the VAT ledgers during 2019, so that the input VAT is included in the monthly VAT settlements for FY 2019.
- The invoices/customs bills are posted in the VAT ledgers in the period January to April 2020: in this case, these documents (to be posted in a separate section of the 2020 VAT ledgers) should be excluded from the monthly VAT settlements of the first four months of 2020, and the related input VAT can be recovered only in the VAT return for FY 2019, due by the end of April 2020.

- The invoices/customs bills are posted in the input VAT ledgers after April 2020: in this case, it might still be possible to recover the input VAT by submitting (at the latest by 31 December 2025, i.e. by the end of the statute of limitations for FY 2019) a supplementary VAT return amending that for FY 2019.

9.6.2 E-invoicing

E-invoicing rules have become mandatory with respect to invoices issued from 1 January 2019.

The transition from paper (e.g. PDF invoices attached to emails) to electronic invoices (i.e. XML invoices transmitted via the SDI) has triggered some practical issues that may impact the right to recover VAT.

- Invoices dated December 2018 and sent to customers by 15 January 2019 can be issued in paper format (and not necessarily through the SDI).
- Invoices dated December 2018 and sent to customers after 15 January 2019 must be issued in electronic format via the SDI.
- Invoices dated January 2019 for supplies made in December 2018 must be issued in electronic format via the SDI.

Invoices dated from 1 January 2019 and issued in paper format are not valid for VAT purposes and have to be treated as not issued. In order to recover the related input VAT the customer should ask the supplier to issue a compliant e-invoice via the SDI. If the supplier does not issue the e-invoice via the SDI, the customer should issue an electronic self-invoice ('autofattura') via the SDI³².

Credit and debit notes dated 2019 and relating to invoices issued in paper format in 2018 must be issued in electronic format via the SDI.

³² The self-invoicing procedure is that indicated in article 6(8) of Legislative Decree no. 471 of 18 December 1997.





9.6.3 VAT errors

VAT is recoverable also when it is charged in error on out-of-scope, exempt or zero-rated transactions, or is charged at an incorrect higher rate, provided that the supplier has remitted the wrongly charged VAT to the Treasury, and that no fraud is involved. If so, the customer will only be subject to a fixed penalty ranging from EUR 250 to EUR 10,000.

Based on the most recent positions taken by the Italian Supreme Court, this rule on VAT recovery, introduced by the 2018 Budget Law, does not apply retrospectively, except to penalties. Under the previous regime, customers were not entitled to recover VAT charged in error, and faced high proportional penalties for unduly recovering VAT and thus submitting inaccurate VAT returns.

9.6.4 Unrecoverable or partially recoverable VAT

There are certain items for which VAT is unrecoverable or only partially recoverable. Some examples are given below.

- **Exempt supplies:** where VAT relates to both taxable and exempt supplies, it must be apportioned.
- **Non-business (including private) activities:** where VAT relates to both business and non-business activities, 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, 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 used in the pursuit of a business activity.
 - The vehicle is used as a taxi.

- The vehicle is used for instruction by a driving school.
- The vehicle is hired out or leased.
- The vehicle is used by sales representatives.
- Since 1 July 2018, input VAT on purchases of fuel and oil and other services related to means of transport can be recovered only if the payment is made through traceable means of payments, i.e. not cash. The following traceable means of payment are admitted: bank and postal cheques; bank and postal promissory notes; electronic means of payment such as direct debits, bank and postal transfers, post-office paying-in slips, debit cards, credit cards, prepaid cards, and any other electronic means that enable direct debiting of a bank account. The following methods typically used by companies in the fuel sector are also allowed, provided that the parties do not pay in cash: netting agreements, cards (rechargeable or not) and vouchers.

- **Business entertainment:** VAT on business entertainment costs is generally not recoverable.
- **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 goods but cannot be recovered on the purchase of those goods.

9.6.5 VAT recovery by non-registered persons established outside Italy

These persons can recover Italian VAT of EUR 50 or more.

Under EU procedures, claimants established in another EU Member State should file an electronic claim with the authorities of their Member State of residence.





A non-EU business should recover VAT under the Thirteenth Council Directive; however, the refund is conditional upon the non-EU state granting comparable turnover tax advantages and 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 EUR 400 or more.

The Thirteenth Council Directive claim forms can be found on the Italian Revenue Agency's website:

www.agenziaentrate.gov.it

9.7 International supplies of goods and services

9.7.1 Exports

Goods

If a seller in Italy sells goods to a customer 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 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.

Upon the entry into force of the UCC, on 16 May 2018 the definition of 'exporter' changed³³: now, an: *"exporter means: a) a private individual carrying goods to be taken out of the customs territory of the Union where these goods are contained in the private individual's personal baggage; (b) in other cases, where (a) does not apply: (i) a person established in the customs territory of the Union, who has the power to determine and has determined that the goods are to be taken out of that customs territory; (ii) where (i) does not apply, any person established in the customs territory of the Union who is a party to the contract under which goods are to be taken out of that customs territory"*.

Services

If a supplier established in Italy provides services to a business customer established in another EU Member State or outside the EU, it makes 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 property³⁴
- passenger transport
- restaurant and catering services
- short-term hiring or leasing of means of transport
- admission (and services ancillary to admission) to cultural, artistic, sporting, scientific, educational, entertainment, or similar activities.

³³ Commission Delegated Regulation (EU) 2018/1063 of 16 May 2018 modifies the definition of exporter contained in article 1(19) of Commission Delegated Regulation (EU) No 2015/2446.

³⁴ The definition of 'services connected with immovable property', given in Council Implementing Regulation (EU) No 1042/2013, has been in use since 1 January 2017.





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 a declaration of intent form to the Italian Revenue Agency and, after obtaining a transmission receipt, must provide its supplier with both the declaration of intent form and the transmission receipt.

The declaration of intent form and instructions can be found on the following website:

www.agenziaentrate.gov.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 settlement covering the period in which the payment is made. This VAT is recovered as input tax in the same VAT settlement.

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

9.8.1 Invoice details

An invoice should contain the following details.

- The date of issue.
- A progressive number that 'unequivocally identifies the invoice' (progressive numbering by calendar year is no longer required). If the invoice adjusts an earlier invoice (in the case of 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 EU Member State, the VAT identification number issued by that Member State.
- For the supplier: company name - or name and surname - and residence or domicile; the company name - or name and surname - and residence or domicile of the tax representative (if any); the location of the fixed establishment (if any) of non-resident enterprises.
- The supplier's VAT number.
- For the purchaser: the company name - or name and surname - and residence or domicile; the company name - or name and surname - and residence or domicile of the tax representative (if any); the location of the fixed establishment (if any) of non-resident enterprises.
- 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 EU Member State, the VAT identification number issued by that Member State.
- The quantity, quality and nature of the goods/ services supplied.





- The tax point date of the supply of goods or provision of services or the date on which the consideration has been wholly or partly paid, if that date is different from the date of issue. This detail should be added to invoices issued as of 1 July 2019.
- The unit price (exclusive of any VAT) which is used to calculate the taxable amount.
- The market value of any goods sold at a discount, whether or not this value is used to calculate 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 has issued the invoice (for self-billed invoices).
- For transactions that are not subject to VAT, the following wording should be used instead of indicating the amount of VAT due:
 - ‘*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 the EU;
 - ‘*autofatturazione*’ (‘self-billed invoicing’), for invoices issued by the buyer of goods or services when this person is liable to pay VAT.

9.8.2 Simplified invoices

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, a simplified invoice may be issued. However, a simplified invoice is not allowed for:

- intra-Community supplies;

- supplies whose place of supply is outside Italy and which are subject to reverse charge in another Member State.

9.8.3 E-invoicing

Up to 31 December 2018 e-invoices were those “issued and received in any electronic format; the use of electronic invoicing is subject to the consent of the customer”³⁵.

The issuer of the invoice should ensure the authenticity of its origin, the integrity of its content and its readability from the moment of issue until the end of the retention period. Authenticity of origin and integrity of content may be guaranteed through one of the following:

- business controls that create a reliable audit trail between the invoice and the supply of goods or services;
- the use of qualified or digital electronic signatures by the issuer;
- electronic data interchange systems;
- other technologies (chosen at the taxpayer’s discretion) that can guarantee the authenticity of the origin and integrity of the data.

From 1 January 2019, e-invoicing is mandatory for all B2B and B2C supplies of goods and services between parties established or resident in Italy (in the case of B2C, only if the customer expressly requests an invoice).

E-invoices must be issued:

- through the SDI, which is the platform originally used to transmit e-invoices to public bodies and which allows the Italian Revenue Agency to automatically collect details of e-invoices;
- in ‘XML’ format, which is the only one currently admitted, although different formats based on European standards might be allowed in the future.

³⁵ Article 21(1) of the Italian VAT Act.





If e-invoices do not fulfil the above conditions, they are considered as not having been issued and there are high penalties (e.g. for domestic taxable supplies, from 90 percent to 180 percent of the VAT in question).

There is a grace period during which penalties for late e-invoicing are applied as follows.

- No penalties apply if a compliant e-invoice is issued (i.e. sent to the SDI) within the 16th of the month after the one in which the tax point is triggered, i.e. within the deadline for the VAT settlement of the relevant month.
- Penalties will be reduced by 80 percent if a compliant e-invoice is issued (i.e. sent to the SDI) within the 16th of the second month after the one in which the tax point is triggered, i.e. within the deadline for the VAT settlement of the second month after the relevant one.

However, the practical application of the grace period (and the duration of this period) depends on the specifics of the case.

Since 1 July 2018 e-invoicing has been mandatory for B2B supplies of:

- gasoline or diesel fuel intended for use as motor fuel for road vehicles (different from those supplied at petrol stations);
- services rendered by subcontractors under a contract with public bodies.

The implementing measures for mandatory e-invoicing and the related technical specifications and clarifications can be found on the Italian Revenue Agency's website:

www.agenziaentrate.gov.it

Electronic invoicing was already compulsory for supplies to public authorities and administrations.

9.8.4 Split-payment system

Sales to public authorities and administrations are governed by a special split-payment regime when suppliers charge Italian VAT (where due, and unless the reverse charge mechanism applies) to public bodies. The public bodies '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.

The split-payment regime also covers:

- supplies of goods and services rendered to certain Italian public bodies, their subsidiaries, and corporations listed on the FTSE MIB Italian Stock Exchange (Borsa Italiana), provided that these corporations are registered for Italian VAT purposes;
- supplies of goods and services rendered to additional categories of public bodies (such as public economic bodies, special companies, foundations, etc.) and their subsidiaries.

To understand if a client belongs to one of the categories covered by the split-payment rule, the supplier should check the lists issued annually by the Italian Ministry of Finance at the link http://www1.finanze.gov.it/finanze3/split_payment/public/#archivio.

Public authorities and administrations are not included in the above lists and reference must be made to the index found on the website:

www.indicepa.gov.it

9.8.5 Self-billing

Self-billing is allowed. However, the supplier remains responsible for issuing the invoice. Furthermore, if the issuer is resident in a low-tax jurisdiction, the supplier (who must have been in business for at least five years and must not have undergone a VAT assessment by the Revenue Agency in the previous five years) must notify the Revenue Agency of the arrangement beforehand.





9.9 Electronic reporting of daily receipts by retailers

It will be mandatory for retailers to electronically record and report their daily receipts to the tax authorities as of:

- 1 July 2019, in the case of retailers whose annual turnover exceeds EUR 400,000;
- 1 January 2020, in the case of all other retailers.

Electronic recording and transmission of daily receipts requires retailers to use a special electronic cash register called a '*registratore telematico*', approved by the tax authorities. Moreover, retailers must issue e-invoices through the SDI if customers request them. Currently, the electronic recording and transmission of daily receipts is mandatory only for certain businesses, e.g. fuel and vending machine businesses.

9.10 Transfers of business

If a business is sold as a going concern, 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.

9.11 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 this case, the reverse charge procedure applies.

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.

9.12 Head office and branch transactions

In sales of **goods**, the local branch and its foreign head office are treated as separate entities for VAT purposes; therefore, no transactions are disregarded.

In the case of **services**, and in light of the ECJ judgment in the FCE Bank case (C-210/04), the Italian Revenue Agency has clarified that transactions between a head office and its branch are disregarded for VAT purposes, on condition that the branch has no decision-making powers. However, due to the changes introduced by the 2018 Budget Law - which, among other things, has implemented the principles set out by the ECJ in the Skandia Case³⁶ - head office to branch charges will no longer be disregarded for VAT purposes when the head office or the branch belongs to a VAT group in Italy or another jurisdiction (see also section 9.4. above).

9.13 Bad debts

In principle, VAT relief can be claimed for bad debts if they are due to a customer's bankruptcy or insolvency and foreclosure procedures are unsuccessful.

Output VAT unpaid by customers who are undergoing bankruptcy and similar procedures is recoverable only **at the end** of the procedure.

³⁶ See footnote 30 on p. 102.





A foreclosure procedure is deemed to have been unsuccessful when:

- a) though ordered, a debtor's assets in the possession of third parties cannot be seized because there are no assets or receivables to seize;
- b) though ordered, moveable goods cannot be seized because goods are missing or because the debtor cannot be found;
- c) after three unsuccessful attempts to sell the goods at public auction, the foreclosure procedure is terminated due to excessive costs.

The European Court of Justice has pointed out that *"a Member State may not make the reduction of the VAT taxable amount in the event of total or partial non-payment subject to the condition that insolvency proceedings have been unsuccessful when such proceedings may last longer than ten years"*³⁷. This statement was issued with specific reference to the Italian system, which appears to conflict with the VAT Directive³⁸. However, the Italian Revenue Agency has not issued any guidelines to implement this judgment.

9.14 Anti-avoidance

There 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 tyres and tyre flaps, livestock, and fresh meat) and is only triggered when the price of the goods is lower than their market value.

Under other anti-avoidance rules, the fair market value becomes the tax basis in certain partially-exempt transactions between related parties.

9.15 Penalty regime

The VAT penalty regime varies according to the type of violation committed by the taxpayer.

VAT return violations

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 to EUR 2,000.

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: 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 failure to invoice certain out-of-scope transactions. The penalty cannot be lower than EUR 500 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 to EUR 2,000.

Failure to apply the reverse-charge mechanism: the penalty ranges from EUR 500 to EUR 20,000. If the transactions are not posted in

³⁷ European Court of Justice judgment of 23 November 2017, in Case C-246/16 (Di Maura).

³⁸ Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax.





the accounting books, the penalty ranges from 5 to 10 percent of the taxable basis and cannot be lower than EUR 1,000.

If the supplier of goods or services fails to issue an invoice, or the invoice contains a mistake, the purchaser is liable to a penalty equal to 100 percent of the 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 to EUR 10,000.

Export-related violations

Penalties apply when a taxpayer does not comply with various rules 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 and the taxpayer can be given a prison sentence ranging from six months to two years.

The same applies to taxpayers who offset more than EUR 50,000 in non-existent or undue VAT credits against tax payments.

General rules

Where the law imposes a range of penalties, the actual amount is established by the Revenue Agency at the time of assessment.

When determining the amount, the Revenue Agency considers 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 Revenue Agency ascertains that the taxpayer has committed similar violations 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 financial year or over several years.

In addition to fines, there are other penalties such as the suspension of trading licences.

Voluntary amendment

The taxpayer can reduce the above penalties (i.e. the penalties that would be due following an ordinary assessment) by using the voluntary amendment system (*ravvedimento operoso*) within a certain time limit.







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.

1. 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.
2. 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 the Union Customs Code, *"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"*³⁹.

The current framework of customs law is a complex structure of national and Community rules, which accumulated as the European integration process developed.

10.1.1 The Union Customs Code

The UCC (Regulation (EU) no. 952/2013 of the European Parliament and of the Council) was adopted on 9 October 2013 and repealed the Community Customs Code (Council Regulation (EEC) No 2913/92). It entered into force definitively on 1 May 2016, and consists of the:

- i. UCC 'Delegated Act' (Commission Delegated Regulation (EU) No 2446/2015), which supplements certain non-essential elements of the UCC;
- ii. UCC 'Implementing Act' (Commission Implementing Regulation (EU) No 2447/2015), which sets out uniform procedural rules for the implementation of the UCC;
- iii. UCC 'Transitional Delegated Act' (Commission Delegated Regulation (EU) No 341/2016), providing for alternative means for the exchange and storage of customs information for as long as the UCC electronic systems are not operational;

³⁹ Article 70 of the UCC.





- iv. UCC “Work Programme”, which took the form of a Commission Implementing Decision, setting out the planning of IT systems.

The UCC is part of the modernisation of customs procedures and is the new framework regulation on customs rules and procedures throughout the EU.

The UCC and the Delegated Act and Implementing Act:

- streamline customs legislation and procedures;
- offer greater legal certainty and standardisation 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 of customs procedures to a paperless and fully electronic environment;
- reinforce swifter customs procedures for compliant and trustworthy AEOs (see below).

With the introduction of the UCC, Community law now requires the paperless exchange of information between different authorities and between authorities and economic operators: all data exchanges must take place using electronic data-processing techniques. This innovation, among others introduced by the Automated Export System (AES)⁴⁰, marks a paradigm shift in customs law, making electronic data exchange the key factor in the relationship between companies and customs authorities.

The UCC stipulates that customs authorities must maintain a regular dialogue with economic operators, promoting transparency by making information about customs law, general administrative rulings and application forms available to the public – free of charge whenever possible⁴¹. It 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.

The UCC also 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*”⁴².

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.

⁴⁰ This system ensures that exports started in one Member State can be concluded in another without the same information having to be submitted.

⁴¹ Article 14(2) of the UCC.

⁴² Article 16 of the UCC.





10.3 Suspensive arrangements and customs procedures with an economic impact (special procedures under the UCC)

Under the UCC, the suspensive arrangements laid down in the repealed Community Customs Code 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.

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

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, 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, 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 allowing 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: i) other charges provided for by other relevant provisions, 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: i) import duties, ii) other charges provided for by other relevant provisions, 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.

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. 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.

10.4 Authorised Economic Operator (AEO)

An AEO is an economic operator that is established in EU customs territory and 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 in the Delegated Act and Implementing Act.

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, terminal operators, 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.

The AEO obtains various direct benefits, including:

- being recognised on the market as a safe and reliable partner;
- easier procedures for 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 clearance⁴³, 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.

The AEO also obtains 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;

⁴³ Provided for in article 179 of the UCC.



- customer loyalty;
- the prevention of problems since employees are known;
- fewer safety-related incidents;
- better planning;
- fewer thefts and losses.

10.5 Binding Tariff Information (BTI) and Binding Origin Information (BOI)

These instruments of the European customs framework can be used by European operators to provide one another with customs classification and origin certainty.

BTI is used to obtain the correct tariff classification for goods that operators intend to import or export.

BOI, on the other hand, is a decision issued by a European customs authority about the actual origin of goods. Once issued, these decisions are binding on the authorities in all Member States in respect of imported or exported goods, provided that the goods and the circumstances determining the acquisition of origin are identical in every respect to the description in the BOI.

Applications for binding information must be made in writing either to the competent customs authority of the Member State or Member States in which the information is to be used, or to the competent customs authority of the Member State in which the applicant is established.

Under the Community Customs Code, BTI was valid for a period of six years from the date of issue, whereas BOI was valid for three years from the date of issue. Under the UCC, however, the

validity period of both BTI and BOI is three years and they are binding not only on the customs authorities but on the applicant as well.

10.6 The Customs Decision System

Starting from 2017, the European Commission launched an innovative Customs Decision System (CDS), to foster further harmonization between Member States and create an online environment for customs decisions.

The system can be accessed through the EU Trade Portal and should be used for specific types of applications to be filed by economic operators. The system will also hold post-application/decision information (e.g. on amendment, revocation, suspension or annulment of decisions).

Currently, the use of the CDS system is mandatory for decisions involving more than one Member State. When a decision affects only one Member State, it can decide whether to allow the use of the CDS system or opt for a domestic system.

10.7 The Registered Exporter System (REX System)

This system simplifies certification of origin of goods and will be applied in the Generalised System of Preferences (GSP), through which the EU unilaterally grants tariff preferences to developing countries, and in specific preferential trade agreements signed by the EU with third countries (e.g. free trade agreement between the EU and Canada and between EU and Japan, which will enter into force on 1 February 2019).





The most innovative change introduced by the REX system is the complete dematerialisation of the certification of origin, which is being replaced by an electronic statement to be issued only by registered exporters⁴⁴.

This major change means that:

- exporters based in GSP countries will have to register for REX purposes in order to make out a valid statement on origin in shipments between GSP countries and the EU;
- European exporters will have to register for REX purposes in order to make out a valid statement on origin under the free trade agreement between EU and Canada and also EU and Japan. Also Canadian and Japanese companies should register for the same purpose;
- European exporters will have to register for REX purposes in certain circumstances.

10.8 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 subject to special rules.

The EU therefore controls the export, transit and brokering of dual-use items that affect the development, 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, setting up a Community regime for the control of exports, transfer, brokering and transit of dual-use items.

10.9 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.

Excise goods are subject to excise duties upon their production or import into the EU. 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;
- they exit (even illegally) a duty-suspension arrangement;
- they are manufactured or imported (even illegally) outside a duty-suspension arrangement.

For the circulation of excise goods, it is necessary to comply with certain formalities, including the lodging of specific documentation.

⁴⁴ The REX requirement is triggered by the exportation of goods whose total value is higher than EUR 6,000.





10.10 Import VAT

In a 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 customs-duty suspension arrangement, if the goods are going to another EU Member State.
- 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 on imports is calculated in accordance with Italian VAT law and customs law.

10.11 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.

The completion of the internal market, the reduction of barriers to international trade and investment, and the greater need to ensure security and safety at the external borders of the Union have changed the role of customs authorities, giving them a leading role within the supply chain and – in their monitoring and management of international trade – making them a catalyst for greater competitiveness on the part of their countries and the companies located in them.

Because of 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).





10.12 Brexit

Reasonably during 2019 the UK is likely to leave the EU, when the period for negotiating a withdrawal agreement ends, unless an extension is agreed.

Although the leaders of the remaining 27 EU countries have endorsed the withdrawal agreement, the UK government, led by Prime Minister Theresa May, is facing opposition in the UK parliament, whose approval is necessary for ratification.

There are three possible scenarios:

- A no deal, which would result in a 'hard Brexit' and, therefore, the United Kingdom's definitive exit from the EU.
- A postponed exit and a possible renegotiation between the parties, through the extension of Article 501 of the TEU (Treaty on European Union).
- A second referendum.

In a 'hard Brexit' the UK would be a third country and all commercial transactions would be relevant for customs purposes. There would be many complications for businesses due to new customs requirements and controls by customs authorities. There would also be a significant increase in costs for supply chain management.

Our Brexit Team is ready and available to help businesses plan an efficient, logical and modern customs model that could minimise the impact of a customs barrier through the use, inter alia, of the special regimes available under the UCC.

10.13 Mr Trump and the EU-US trade war

On 8 March 2018 the President of the United States, Donald Trump, decided to introduce duties of 25 percent and 10 percent respectively on steel and aluminium imports, which entered into force on 23 March 2018.

The EU responded with countermeasures, by introducing other duties through Commission Implementing Regulation (EU) 2018/886. Since 22 June 2018, the products listed in Annex I of this regulation have been subject to additional 10 percent and 25 percent *ad valorem* duties on imports from the United States.

These measures will remain in force as long as the US customs duties on goods from the EU continue to be applied. The products concerned include, for example: vegetables and legumes; rice; fruit juices; tobacco; make-up products; various woven garments; various products made of steel, tin, aluminium, cast iron and tin; motorcycles (including mopeds); yachts and other ships and boats; playing cards.

The regulation provides for the launch of a possible second phase in which, on imports of the products indicated in Annex II, *ad valorem* duties of 10 percent, 25 percent, 35 percent and 50 percent will be applied.

The date of entry into force of these further countermeasures is 1 June 2021 or - if earlier - the fifth day after the date on which the World Trade Organization takes a decision about them. In this second case, the Commission will publish a notice in the Official Journal of the European Union to announce the date of adoption or notification of that decision.





None of the additional duties will be applied in cases where:

- an import licence, involving an exemption from or a reduction in the duty, was issued before Regulation (EU) 2018/886 came into force;
- the importer can demonstrate that the export from the United States to the EU took place before the date of application of the additional duty.

10.14 New definition of exporter

In late 2018 the Italian Customs Authority issued clarifications⁴⁵ about the new definition of exporter introduced by the EU⁴⁶.

The new definition seems to be simpler than the previous one: even if the requirement of establishment in the customs territory of the Union is still required, in order to qualify as an exporter it is sufficient for the person to decide that the goods must leave the EU customs territory.

The new rule also covers situations where it is not possible to identify an exporter, e.g. when the power to decide that the goods must leave the EU customs territory is exclusively in the hands of the purchaser established in a third country, as in contracts with *ex works* delivery terms.

In such cases the exporter may even be a person established in the customs territory of the Union who is party to the contract under which the goods are to be taken out of the customs territory, e.g. the seller or the carrier⁴⁷.

The Italian Customs Authority points out that, following the rewording of the definition, the provision which allowed for the application of transitional measures no longer includes the possibility that “*a person not established in the customs territory of the Union may be indicated in box 2 of the customs declaration as consignor, provided that the customs declaration is lodged by a representative established in the EU, acting as an indirect customs representative*”.

⁴⁵ On 17 October 2018 the Italian Customs Authority published Statement of Practice no. 112029, a few months after the publication of the UCC guidelines on the new definition of exporter, published on 30 July 2018.

⁴⁶ Article 1 (19) (b) (i) of Commission Delegated Regulation (EU) 2015/2446 of 28 July 2015 supplementing Regulation (EU) No 952/2013 of the European Parliament and of the Council as regards detailed rules concerning certain provisions of the Union Customs Code.

⁴⁷ Article 19 (b) (ii) of Commission Delegated Regulation (EU) 2015/2446.







11. Tax dispute resolution

11.1 Official procedures enabling dialogue with the tax authorities

11.1.1 Ordinary tax rulings

In Italy there are five types of tax rulings.

- 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 apply⁴⁸.
- d) *'Interpello antiabuso'*, to understand whether the new abuse of law rule applies to one or more transactions⁴⁹.

- 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 Revenue Agency may respond after this deadline. Only in the case of an *'interpello ordinario'* and *'interpello qualificatorio'* must the Italian Revenue Agency reply within 90 days. For other categories of ruling, the Italian Revenue Agency must reply within 120 days. In all cases, if the Revenue Agency requires additional documentation, the response time can be deferred by 60 days, only once.

If the Revenue Agency does not respond within the above time frames, the solution proposed by the taxpayer is deemed to have been accepted by the Revenue Agency.

⁴⁸ See the section headed *'Controlled foreign company rule'* in section 5.

⁴⁹ See the section headed *'General anti-avoidance rule'* in section 5.





11.1.2 Substantial investment ruling

A specific form of tax ruling is available for companies that intend to invest a minimum of EUR 30 million in Italy, generating new employment. However, the 2019 Budget Law has reduced the investment threshold to EUR 20 million for tax rulings submitted as of 1 January 2019. The idea is to provide greater certainty about the income generated by such investment plans and the wider tax implications. Together 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, e.g. whether abuse-of-law or other anti-avoidance measures are likely to be triggered, the tax implications of a group reorganisation, whether certain assets constitute a going concern. The Revenue Agency should provide the investor with a written answer within 120 days. If it does not, the solution proposed by the taxpayer is deemed to have been accepted. The answer is binding as long as the facts and circumstances do not change.

11.1.3 Fast-track ruling under the cooperative compliance regime

MNEs that have an effective tax control framework (i.e. those equipped with an adequate system for mapping, measuring, preventing and managing tax risks, as well as internal systems enabling clear definition of roles and responsibilities within the organisation) are eligible to opt for the Italian cooperative compliance regime, provided that they satisfy one of the following conditions.

- Their turnover (or income) exceeds EUR 10 billion.
- Regardless of their turnover, they have obtained a tax ruling on substantial investments.
- They have disclosed the existence of an unreported permanent establishment to the Revenue Agency and settled this issue with it.

The taxpayer may opt for the regime by submitting an electronic application. Following the Revenue Agency's confirmation, communicated within 120 days of the application, the regime runs from the financial year in which the application has been submitted.

One of the benefits offered by the Italian cooperative compliance regime is the fast-track advance ruling request, to which the Revenue Agency must reply within 45 days (instead of the 90-120 days for a standard ruling). Other benefits of the regime are listed below.

- It allows a continuous exchange of information between the Revenue Agency and taxpayers, with a view to preventing tax litigation.
- It allows taxpayers to evaluate any potential tax risks with the Italian Revenue Agency before the deadlines for their tax returns.
- Administrative sanctions can be reduced by 50 percent and collection of these sanctions is suspended until final assessment.
- If the taxpayer is accused of a tax crime, the Italian Revenue Agency will inform the public prosecutor that the taxpayer has adhered to the cooperation regime.





11.1.4 International ruling

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 DTT 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 the activity that an MNE intends to pursue in Italy may trigger a permanent establishment in Italy, under Italian tax law and DTTs;
- 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 State⁵⁰.

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.

Before filing an application, taxpayers may ask for a meeting with the Revenue Agency (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 Revenue Agency, to let the Revenue Agency verify compliance with the agreement.

⁵⁰ See the section headed 'Moving tax residence to Italy: tax basis of assets and liabilities' in section 5.





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. 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.

11.1.5 Advance pricing agreements

Bilateral and multilateral APAs are available (even if not regulated by any specific law) and are binding for five years, while international rulings, with respect to transfer pricing matters – see above – are a form of unilateral APA.

11.2 Tax audits

11.2.1 Statute of limitations

Under ordinary rules, a financial 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 of FY 2016, a financial 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 financial year follows the calendar year, FY 2015, the tax return for which is filed in 2016, will become time-barred on 31 December 2020, but FY 2016 will become time-barred on 31 December 2022). If the tax return is not filed, the statute of limitations is extended by one year for assessments of financial years up to and including FY 2015, and by two years for assessments of FY 2016 and beyond.

For assessments of financial years up to and including FY 2015, if tax inspectors detect a violation that could constitute a criminal tax offence, and inform the public prosecutor before the ordinary statute of limitations expires, the time limit doubles for assessment purposes (e.g. FY 2015 becomes time-barred on 31 December 2024). Starting with assessments of FY 2016, this extension will no longer apply (i.e. FY 2016 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 to which equivalent rules apply (e.g. cadastral and mortgage tax), the authorities can assess additional taxes within two or three years (based on the type of alleged violation) of the date the deed (e.g. a contract) is filed for registration. If the deed has not been filed for registration, authorities can assess taxes within five years of the day the deed was supposed to be registered.

11.2.2 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. Additional 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 after the issue date of the audit report. This is to allow the taxpayer time 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 time limit 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, after the notice of assessment has been served, initiate litigation proceedings under one of the following procedures (this list is not exhaustive and merely represents those procedures applied most commonly).

Pre-hearing compromise

Either before or after the notice of assessment is served, the taxpayer can apply 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 application is never binding (i.e. it does not oblige the parties to reach an agreement).

If a pre-hearing compromise is reached, the ordinary penalties for the purported violations are reduced to one-third of the tax adjustment agreed upon in compromise.

A pre-hearing compromise application submitted after the final notice of assessment has been served has the effect of extending the appeal deadline (ordinarily 60 days) by an additional 90 days (to 150 days in total). A taxpayer who files an application for a pre-hearing compromise before the notice of assessment is served, and who fails to reach a settlement, cannot file another application after the notice of assessment has been served. In this case, the 90-day extension is not granted.

Mediation

The taxpayer must launch advance mediation proceedings in response to all notices of assessment involving sums of up to EUR 50,000. Mediation is compulsory and an appeal is barred if no mediation attempt is made. If the mediation procedure is unsuccessful, the taxpayer may start litigation. If an agreement with the authorities is reached during the mediation procedure, penalties are reduced to 35 percent of the agreed level of adjustment.





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 is 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. Decisions of the tax courts are provisionally executive, thus requiring provisional repayment to the party that wins the case at the first or second level of adjudication.

The appeal must be filed within 60 days of the date on which the notice of assessment is served. If a pre-hearing compromise is requested (and was not requested before the final notice of assessment), an additional 90 days will be granted to file the local court appeal (see above).

The appeal does not suspend provisional collection, which can start after 180 days, when the notice of assessment becomes enforceable. In any event, the taxpayer can submit an application to the local court to have collection suspended if certain conditions are met.

If, instead, the taxpayer accepts the notice of assessment without appeal by paying the amount demanded within 60 days, penalties are reduced to one-third of that amount.

Judicial conciliation (compromise after appeal)

After an appeal has been filed, the taxpayer (as well as the tax authorities) may still apply to start a partial or total judicial conciliation process.

If a compromise is reached before the local tax court hearing, penalties are reduced to 40 percent of the agreed level of adjustment.

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 amendment (*ravvedimento operoso*)

After an audit has ended, but before the notice of assessment is served, the taxpayer can correct mistakes identified in the audit report by paying the corresponding tax. In this case, penalties are reduced to one-fifth of the minimum amount. If the voluntary amendment application is filed before the audit ends, penalties are reduced to one-sixth.

11.2.3 Temporary tax amnesties

In October 2018 a package of tax measures was introduced, allowing taxpayers to settle tax demands with certain reductions.

The main measures, for which taxpayers can still opt, are summarized below.

Settlement of a tax audit report

Taxpayers may settle taxes demanded in a tax audit report (PVC) issued by 24 October 2018, without paying any penalties or interest. In order to opt for this settlement, taxpayers must submit a supplementary tax return and pay the taxes (at least the first installment) by 31 May 2019.

Settlement of liabilities

Taxpayers may settle tax liabilities dating from FY 2000 to FY 2017 and already assigned to the tax collector, without paying any penalties or interest on arrears. In order to opt for this settlement, taxpayers must submit a special application to the tax collector by 30 April 2019, abandon any pending litigation, and pay the taxes (at least the first installment) by 31 July 2019.





Settlement of pending tax disputes with the Italian tax authorities

Taxpayers may settle tax disputes with the Italian tax authorities, pending on 24 October 2018, by paying all or part of the taxes charged, without any interest or penalties. The payments to settle the litigation depend on the provisional decisions already obtained by the taxpayer from the courts. In order to opt for this settlement, taxpayers must submit a special application and pay the amounts due (at least the first installment) by 31 May 2019.

11.2.4 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 result in double taxation. There are two instruments in place to remove double taxation: one is a MAP initiated under the European Arbitration Convention (typically activated when adjustments affect two or more European jurisdictions), the other is a similar procedure initiated under the applicable DTT (open to private individuals and non-European jurisdictions).

Procedures initiated under the Arbitration Convention give certainty of double taxation removal: if the competent authorities do not reach an agreement, a second arbitration phase begins, during which a decision on the final adjustment is always made. This is not the case under DTTs as, with the exception of the few conventions that contain arbitration clauses, the competent authorities must only endeavour to reach an agreement.

A relevant factor is how a MAP initiated under the Arbitration Convention interacts and conflicts with litigation before the Italian tax court. The competent Italian authorities take the view that when a local tax court delivers a decision, they are not obliged to accept the outcome of a 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 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 a seller resident in Italy – the capital gain being the difference between the sale price and tax basis of the shares – may be partially exempt from tax, provided that the Participation Exemption requirements are met.

The buyer cannot obtain tax recognition of the amount paid for the shares over and above the underlying net book value of the target: in other words, the tax bases of the target's assets and liabilities remain unchanged after the acquisition. However, on certain conditions, the buyer can obtain tax recognition of the higher value of the intangible assets included in the underlying value of the shares acquired (and recognised in the consolidated financial statements) by paying a 16 percent substitute tax. Starting from the financial year running on 31 December 2017, these rules have been extended to the acquisition of shares in non-resident companies.

The 2019 Budget Law extends the deadline for the optional step-up of the tax basis of shares in unlisted companies, held on 1 January 2019 by a non-resident entity (without a permanent establishment in Italy). This step-up is subject to the payment of a substitute tax on the cost, to be appraised by 1 July 2019. The substitute tax must be paid, by 1 July 2019 or in three equal annual installments, as follows:

- 11 percent in the case of qualifying shares
- 10 percent in the case of non-qualifying shares.

As a capital gain realised from 1 January 2019 will be subject in full to a 26 percent substitute tax, this step-up regime could be advantageous for non-residents (without a permanent establishment in Italy) which sell shares in unlisted Italian companies and which cannot benefit from DTT relief. The above taxation of capital gains applies unless the seller is eligible for a DTT that stipulates otherwise. The sale of shares is not subject to VAT but is generally subject to a fixed registration tax of EUR 200.

The transfer of shares in a company incorporated in Italy as an S.p.A. or S.a.p.a. is subject to a financial transaction tax (Tobin tax) at a standard 0.2 percent rate, on 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 quotas in a company incorporated as an S.r.l.





The transaction value generally means the purchase price, the net balance of transactions involving the same financial instrument and concluded on the same day by the same party, the price contracted, or, failing that, the fair market value determined according to consolidated income tax rules.

There are certain exemptions from the financial transaction tax, e.g. shares transferred between related parties or share transfers related to restructuring operations as defined by article 4 of Council Directive 2008/7/EC.

12.1.2 Asset deals

An asset deal allows the buyer to acquire only the business unit 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 for infringements committed in the year when the transaction takes effect or the two previous years or for infringements already assessed by the tax authorities or under assessment in the same period, although committed in previous years. It is possible to obtain a clearance certificate from the Italian tax authorities, attesting the extent of the tax liabilities for which joint tax exposure exists. In this case, the buyer's liability is limited to the amount 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 business unit acquired is its purchase price. The seller realises a taxable capital gain equal to the difference between the sale price and the tax basis of the business unit. The 24 percent 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 pays tax on the full 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 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 unit 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 unit 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 unit 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 (IRES of 24 percent on five percent of the capital gain).

From a buyer's perspective, the NewCo offers the option (as an alternative to the ordinary tax regime) of realigning the tax basis of the business unit with its book value, 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 the amount between EUR 5 and EUR 10 million
- 16 percent on any further amount.

The stepped-up assets are subject to ordinary tax rules on amortisation/depreciation. 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
- brands or trademarks
- other intangibles (with an indefinite useful life)
- controlling interests (if certain conditions are met).

This 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 instead of 18, regardless of the amortisation charged to the P&L account. The increased tax basis is recognised from the second financial year following the transaction.

The contribution of a business unit is not subject to VAT. A fixed registration tax of EUR 200 is due.

Contributions of going concerns followed by a sale of shares/quotas used to be recast by the tax authorities as transfers of assets (article 176 deals).

This led to claims for registration tax, ranging from 3 percent to 9 percent, as opposed to the fixed EUR 200 tax due on transfers of shares/quotas. The 2018 Budget Law clarified that tax offices should have imposed registration tax on each deed separately, without considering any other deeds executed immediately after the transaction, and that step transactions can be challenged only through the general anti-abuse rules. The 2019 Budget Law specifies that the clarification introduced by the 2018 Budget Law is retroactive and therefore applies also to deeds executed and registered before 1 January 2018.

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. Tax neutrality 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 step-up 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 carryforwards) of the companies involved in the merger are subject to the following tests.

- **Business vitality test:** the P&L 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 carryforwards 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, these limits do not apply in the event of a merger between entities that are part of the same tax group.

Since 1 January 2017 it has also been possible to carry forward any surplus ACE, subject to the business vitality test and net equity test. However, as the 2019 Budget Law repeals the ACE regime from 1 January 2019, this rule now applies only to any surplus ACE deduction accrued up to 31 December 2018.

The tax effects of the merger can be backdated to the beginning of the financial 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 and interest carryforwards of the interim period.

A merger is not subject to VAT. In general, each merger is subject to a fixed registration tax of EUR 200.

Mergers may be scrutinised for anti-avoidance purposes.

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.

Tax neutrality has the following implications.

- Demerger differences (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 (e.g. tax deferrals on capital gains realised in previous years, tax loss carryforwards) 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 tax-deferred reserves 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 loss carryforwards 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.

Since 1 January 2017, it has also been possible to carry forward any surplus ACE and interest carryforwards, subject to the business vitality test and net equity test. However, as the 2019 Budget Law repeals the ACE regime from 1 January 2019 this rule now applies only to any surplus ACE deduction accrued up to 31 December 2018.





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 fixed registration tax of EUR 200 is due.

Especially when real estate was transferred, the Italian tax authorities used to recast a demerger followed by the disposal of shares in the beneficiary company (two separate transactions usually subject to a fixed registration tax of EUR 200 each) as a sale of a going concern, and demand additional proportional registration tax. The 2018 Budget Law clarified that the tax offices should have imposed registration tax on each deed separately, without considering any other deeds executed immediately after the transaction, and that step transactions can be challenged only through the general anti-abuse rules. The 2019 Budget Law specifies that the clarification introduced by the 2018 Budget Law is retroactive and therefore applies also to deeds executed and registered before 1 January 2018.

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 latter case, 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 Markets in Financial Instruments Directive (MiFID II) entered into force on 3 January 2018.

The main markets available in Italy for the listing of shares are the following.

- Mercato Telematico Azionario – MTA:** this is Borsa Italiana's main market, 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 the one hand and retail investors on the other, 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 of at least EUR 40 million and a free float of at least 25 percent (35 percent in the case of STAR companies). The substantive requirements include a sound and clear strategy, a good competitive advantage, a balanced financial structure, managerial autonomy, and all of the factors that help to improve 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 must comply with specific governance requirements. The companies listed on the MTA and the MIV (Market for Investment Vehicles) 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 MTA indices, also have their own specific index.





Within the MTA market is the STAR segment, dedicated to middle-sized 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
 - high liquidity (minimum free float of 35 percent)
 - corporate governance requirements in line with international standards.
- **AIM Italia:** this is the Borsa Italiana market devoted to Italian SMEs with high growth potential. The market was born on 1 March 2012 from the merger of the AIM Italia and MAC (Mercato Alternativo del Capitale) markets, 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 the know-how obtained from more than 15 years of experience of the British AIM on the one hand 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, thanks to an efficient regulatory system that meets the needs of small businesses and specialised investors. It is not necessary to publish a prospectus to gain admission and it is not necessary to publish quarterly management reports afterwards. Companies applying to AIM Italia must appoint a nominated adviser from an approved register held by Borsa Italiana. The nominated advisor 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 more quickly 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, allowing them to benefit from international visibility and enjoy 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 SMEs.
 - The nominated adviser, who supports a company during the admission phase and throughout its time on the market, and who is of central importance.
 - Easier admission requirements than for the primary market: AIM Italia sets 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.
- **Borsa Italiana Equity MTF:** this includes the Global Equity Market (GEM), which substituted the MTA-International segment and is dedicated to the trading of shares of non-Italian issuers already traded on regulated markets in EU Member States or in other OECD member countries.

The following table illustrates the main admission and ongoing requirements for MTA and AIM Italia.



	MTA	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 / Management Information System / Business Plan / Quota Management Admission Test	Admission document
Market cap	Min. EUR 40 million	No formal requirements
Board of directors (independent directors)	Recommended (Corporate Governance Code)	No formal requirements
Internal audit committee	Recommended (Corporate Governance Code)	No formal requirements
Remuneration committee	Recommended (Corporate Governance Code)	No formal requirements
Incentives to top management	Recommended (Corporate Governance Code)	No formal requirements
Investor relator	Recommended	Not mandatory
Website	Mandatory	Mandatory
Main advisor	Sponsor / Global coordinator	Nominated advisor
Key continuing obligations		
Corporate governance	Comply or explain	Optional
Specialist	Optional (liquidity provider)	Mandatory (liquidity provider)
Disclosure	Price-sensitive information and M&A (TUF ⁵¹ and CONSOB Rules on Issuers)	Price-sensitive and extraordinary operations
Takeover code	-	Public take-over bid
Related parties	Procedures and reporting requirements	Easy procedures and disclosure obligations
Quarterly data	First-quarter, second-quarter and third-quarter report within 45 days of the quarter end	No
Half-year data	Within 60 days of the half-year end	Within 3 months of the half-year end
Annual report	Within 120 days of the year end	Publication within 6 months of the year end

⁵¹ The Consolidated Law on Finance (Legislative Decree no. 58/1998).





Glossary

TERM	DEFINITION
2016 Stability Law	Law no. 208/2015
2017 Budget Law	Law no. 232/2016
2018 Budget Law	Law no. 205/2017
2019 Budget Law	Law no. 145/2018
ACE	Allowance for corporate equity
Anagrafe	The Office of Records of the Resident Population in Italy
APA	Advance pricing agreement
B2B	Business-to-business
B2C	Business-to-consumer
BEPS	Base erosion and profit shifting
Borsa Italiana	Borsa Italiana S.p.A. (Italy's main stock exchange)
CFC	Controlled foreign company
CFC rule	Anti-avoidance rule that applies to the Italian controlling shareholder of certain CFCs
CIT	Corporate income tax (in Italy this is IRES)
CONSOB	<i>Commissione Nazionale per le Società e la Borsa</i> (National Commission for Companies and the Stock Exchange)
Cooperative jurisdiction	A jurisdiction that allows an adequate exchange of information with Italy
DTT	Double tax treaty
EBITDA	Earnings before interest, taxes, depreciation and amortisation
ECJ	European Court of Justice
EEA	European Economic Area
EIB	European Investment Bank
EIF	European Investment Fund
EU	European Union
FIFO	First-in first-out accounting method





FY	Financial year
GAAP	Generally Applied Accounting Principles
GDP	Gross domestic product
IAS	International Accounting Standards
IFRS	International Financial Reporting Standards
INPS	<i>Istituto Nazionale della Previdenziale Sociale</i> (National Institute of Social Security)
Interest and Royalties Directive	Council Directive 2003/49/EC of 3 June 2003
IoT	Internet of things
IP	Intellectual property
IRAP	<i>Imposta regionale sulle attività produttive</i> (regional business tax)
IRES	<i>Imposta sul reddito delle società</i> (corporate income tax)
IRPEF	<i>Imposta sul reddito delle persone fisiche</i> (personal income tax)
ISTAT	<i>Istituto Nazionale di Statistica</i> (Italian National Institute of Statistics)
ITC	Income Tax Code (TUIR – <i>Testo Unico Imposte sui Redditi</i> – Presidential Decree no. 917/1896)
IVAFAE	<i>Imposta sul valore delle attività finanziarie detenute all'estero</i> (tax on the value of financial assets held abroad)
IVIE	<i>Imposta sul valore degli immobili situati all'estero</i> (tax on the value of real estate held abroad)
LIFO	Last-in first-out accounting method
M&A	Mergers and acquisitions
MAP	Mutual agreement procedure
MNE	Multinational enterprise
NewCo	New company
Non-qualifying share/ shareholding	See table in section 5.2.6. on p. 66
OECD Model Tax 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
OIC	<i>Organismo Italiano di Contabilità</i> (the Italian accounting body)
P&L	Profit and loss
Parent-Subsidiary Directive	Council Directive 90/435/EEC of 23 July 1990, amended by Council Directives 2003/123/EC and 2011/96/EU of 30 November 2011 (recast)





Participation Exemption	The tax exemption for qualifying dividends and capital gains realised on disposals of shares 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
Qualifying share/ shareholding	See table in section 5.2.6 on p. 66
Quota/quotas	An equity interest in an Italian S.r.l. company
R&D	Research and development
Redditi PF return	The income tax return for individuals
Redditi SC return	The income tax return for corporates
SDI	<i>Sistema di interscambio</i> (the official electronic exchange/transmission system)
SMEs	Small and medium-sized enterprises
SPV	Special purpose vehicle
TFR	<i>Trattamento di Fine Rapporto</i> (employee's end-of-service allowance)
UCC	Union Customs Code
VAT Act	Presidential Decree no. 633/1972
WHT	Withholding tax
YoY	Year on year

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For further information:

Ancona

Via I Maggio, 150/A - 60131
T: +39 071 2916378

Aosta

Regione Borgnalle, 10 - 11100
T: +39 016 5267118

Bari

Via Abate Gimma, 62/A - 70121
T: +39 080 5243203

Bergamo

Via Camozzi, 5 - 24121
T: +39 035 240218

Bologna

Via Innocenzo Malvasia, 6 - 40131
T: +39 051 4392711

Bolzano

Via della Rena, 20 - 39100
T: +39 0471 1324010

Brescia

Via Cefalonia, 70 - 25124
T: +39 030 2425720

Catania

Via Genova, 49 - 95127
T: +39 095 449397

Como

Via D. Fontana, 1 - 22100
T: +39 031 261866

Firenze

Viale N. Machiavelli, 29 - 50125
T: +39 055 261961

Genova

P.zza della Vittoria, 15/12 - 16121
T: +39 010 5702225

Lecce

Via Imbriani, 36 - 73100
T: +39 0832 317930

Milano

Via Vittor Pisani, 25/27/31 - 20124
T: +39 02 676441

Napoli

Via F. Caracciolo, 17 - 80122
T: +39 081 662617

Novara

Via Cairoli, 4 - 28100
T: +39 032 1613571

Padova

P.zza Salvemini, 2 - 35131
T: +39 049 8239611

Palermo

P.zza Castelnuovo, 50 - 90141
T: +39 091 6111445

Parma

Viale G. Falcone, 30/A - 43100
T: +39 052 1236211

Perugia

Via Campo di Marte, 19 - 06124
T: +39 075 5734518

Pescara

P.zza Duca d'Aosta, 31 - 65121
T: +39 085 4210479

Roma

Via Adelaide Ristori, 38 - 00197
T: +39 068 09631

Torino

C.so V. Emanuele II, 48 - 10123
T: +39 011 883166

Treviso

Via Rosa Zalivani, 2 - 31100
T: +39 042 2576711

Trieste

Via P. da Palestrina, 12 - 34133
T: +39 040 3480285

Varese

Corso Matteotti, 1 - 21100
T: +39 033 2282356

Verona

Via Leone Pancaldo, 68 - 37138
T: +39 045 8114111

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Printed in Italy.

Publication date: March 2019

Graphic: New! srl - www.newadv.com