

LEGAL INFORMATIVE NEWSLETTER

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We are pleased to provide you with the new issue of our legal information newsletter.

Topical legal questions are discussed and those related to issues that you might encounter.

We hope that you will find it of interest. We would welcome any comment you might have.

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**ITALIAN TAX SYSTEM – OVERVIEW OF THE MAIN EUROPEAN AND DOMESTIC STATUTORY REGULATIONS ON TAXES**

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**§ 2 TAX SYSTEM**

**§ 1.1 Corporate Income Tax (IRES)**

Corporate income tax (IRES) is regulated by the Unified Text on direct Taxes (*“Testo Unico Imposte Dirette”*).<sup>1</sup> Italian resident corporations are subject to IRES on their worldwide income. Non-Italian resident corporations are subject to IRES only on Italian source income.

As of January 1, 2004, the imputation system previously in force has been abolished and replaced with the so called 'partial exemption' method, under which corporate profits are subject to income tax at the level of the company and partially exempted at the level of the shareholders.

In addition, other significant measures have been introduced, e.g. reductions in corporate income tax, the participation exemption regime and the domestic tax consolidation regime.

**§ 1.2 Taxable persons, tax rates and taxable period**

Corporate Income Tax (IRES) applies to resident and non-resident corporations. Resident

corporations are subject to IRES on their worldwide income, so-called 'unlimited taxation'.

Non-resident entities are subject to IRES only on income considered sourced in Italy, 'limited taxation'.

Resident corporations include Corporations (*“Società per azioni - Spa”*), Limited liability companies (*“Società a responsabilità limitata – Srl”*), and Partnerships limited by shares (*“Società in accomandita per azioni- Sapa”*).

Resident corporations also include companies formed under foreign jurisdictions, which, for most of the taxable period, have their statutory office, place of effective management, or main object of their business in Italy.

Resident partnerships not limited by shares, are not subject to IRES. Such partnerships, namely *“società in nome collettivo - Snc”*, or *“società in accomandita semplice - Sas”*, are considered transparent entities.

For tax purposes, their income is attributed to the partners and subject to tax accordingly.

For IRES purposes, the taxable period coincides with the company's financial year, as provided by the law or by the articles of association. Otherwise, the taxable period coincides with the calendar year.

IRES is levied at a flat rate of 27,5%.<sup>2</sup>

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<sup>1</sup> Act No. 917/86.

<sup>2</sup> Act No. 917/86.

### § 1.3 Regional tax on business activities (IRAP)

Regional tax on business activities, “*Imposta regionale sulle attività produttive – IRAP*”, is a local tax applied on the value of the production generated in each taxable period by persons carrying out business activities in a given Italian region.

Non-Italian resident corporations are subject to IRAP only on the production generated through Italian permanent establishments. Rates may vary, though they range around 3.9%.

### § 1.4 Indirect taxes – Value Added Tax (VAT)

The Italian value-added tax (VAT) system conforms fully to European Union VAT rules. In principle, the system ensures that VAT is borne by the ultimate consumer only and that, at the upper level, input VAT is deducted by the suppliers of goods and of services. VAT is charged on any supply or service deemed to be made or rendered within the Italian territory.

The ordinary VAT rate is set at 22%.<sup>3</sup>

### § 1.5 Transfer tax

Transfer tax (“*Imposta di registro*”), is due on specific contracts if formed in Italy, and contracts including those formed abroad, regarding the transfers or leases of business concerns or immovable properties situated within the Italian territory. The taxable base and rates depend on the nature of the contracts and on the status of the parties.

When transferring immovable properties, cadastral and mortgage taxes also apply.

These are due for formal transcription in the public registers. The tax base matches that of the transfer tax, with tax rates set respectively at 1% and 2%.

Transfer tax, cadastral and mortgage taxes are imposed as a lump sum of €129.11 on transfers

of immovable properties subject to VAT. Alternatively, transfer tax rates may vary from 4% up to 15% depending on the type of real property.

### § 1.6 Municipal tax on real estate

Any owner, resident or non-resident, of real properties located within Italian territory must pay annually the municipal tax on immovable property, “*Imposta Municipale Unica - IMU*”. This tax is levied at two rates 0.4 % on the value main residences and 0.76% on the value of most other properties. Local authorities can slightly change these rates within their district by + or - 0.2%, by issuing local regulations.

The main residence (*Abitazione principale*) reduced rate of tax (0.40%) is only applicable to actual, habitual abode (*Dimora*) of the taxpayer and his family, provided this appears on public records (*Residenza anagrafica*).

For most residential units, IMU tax will be levied on a statutory property value, calculated by multiplying the land registry income (as it was in the official Italian land registry records for the relevant property on 01.01.2012) by 5 and then by 160. Different figures apply to offices, factories and shops.

### § 1.7 Inheritance tax and gift tax

On December 24, 2007 new rules were enacted to regulate inheritance and gift taxes.<sup>4</sup>

The inheritance and gift tax is imposed on the value of the share of each beneficiary. The rates vary depending on the relationship between the deceased and the beneficiary, as well as the non-taxable threshold amount.

Inheritances of spouses and direct descendants or ascendants are subject to inheritance tax at a rate of 4% on the amount exceeding €1,000,000 per beneficiary.

Transfers to brothers or sisters are taxed at 6% on the amount exceeding €100,000 per beneficiary.

<sup>3</sup> Act No. 633/72.

<sup>4</sup> Act No. 244/07.

Transfers to relatives up to the fourth degree or relatives-in-law up to the third degree are taxed at 6% on the entire amount of their inheritance.

Any other transfer is taxed at 8% on the entire amount.

## § 2 FOREIGN INVESTMENT

### § 2.1 Registrations and Permits

There are not specific statutory regulations in Italy providing limitations on foreign investment in the Country. In principle, foreign investments as well as domestic investments can be forbidden only for reasons of public order, public health or other general principles of law.

[A] EU Citizens and EU companies – In accordance with the general principles of EU, foreign EU citizens and EU companies enjoy the same treatment and protection of law as domestic ones.

[B] NON EU Companies – As long as the reciprocity of treatment with another Country is observed, foreign companies are generally allowed to operate, to maintain representative offices or permanent establishments, to incorporate subsidiaries and to participate to domestic business concerns in Italy.

### § 2.2 Transfer of dividends, interest and royalties abroad

Transfer of dividends, interest and royalties abroad is not restricted. As tax statutory regulations set forth, foreign citizens with fiscal residence in Italy or companies incorporated in Italy or foreign companies without fiscal residence in Italy but having there a permanent establishment, are taxable subjects in Italy and have to pay taxes in accordance with the relevant tax statutory regulations applicable.

Definition of permanent establishment substantially matches the definition that Article 5 of the OECD Model Convention (double taxation) establishes.

Dividends, interest and royalties paid to foreign citizens or foreign companies without fiscal

residence in Italy, but with a permanent establishment, are taxed through a withholding tax.

### § 2.3 Withholding taxes on foreign investments (dividends, interest and royalties)

There are three main withholding taxes applicable at source on certain payments: dividend withholding tax, withholding tax on interest, and withholding tax on royalties.

[A] **Dividend withholding tax** – Dividends received from the 1st of January 2012 by individuals outside the scope of a business activity are subject to a 20% withholding tax in settlement of whereby they concern non qualifying holdings. Qualifying holdings consist of shares (other than savings shares) and any other investment in the capital or equity of a company to which voting rights are linked in the ordinary Shareholders’

Meeting exceeding 2% or 20%, if the securities are traded on a regulated market, or 5% or 25% in other cases.

Dividends received from the 1st of January 2012 by individuals outside the scope of a business activity regarding a qualifying holding in Italian companies are not subject to withholding tax, whereas those regarding foreign companies are subject to a 20% withholding tax on account for the taxable portion of profit – i.e. 49.72% of the total (with a consequent filing requirement and deduction of any credit for taxes paid abroad), net of any withholding tax applied in the foreign country. In applying the withholding, account is taken of double taxation agreements, which could provide for the reduction or elimination of the tax.

If dividends are distributed to a foreign company resident in a State under a privileged tax regime (tax havens), they shall be subject to taxation in full, unless the taxpayer receives a positive response to an opinion request (interpello) from the Revenue Agency.

From the 1st of January 2012, dividends received by parties other than individuals not resident in Italy are generally subject to a 20% withholding

tax in settlement. However, whereby non resident parties are companies or entities subject to corporate income tax in the countries entered in the so-called white list, the rate is equal to 1.375%.

Reduced rates are possible under any tax treaties, Italy has concluded with the recipients' country of residence.

The withholding tax is not due, in line with the EU Parent-Subsidiary Directive, for dividends paid by Italian resident corporations to its EU parent company. The benefit is subject the parent's current ownership dating back at least one year, of no less than 25% of the Italian subsidiary's share capital.

**[B] Withholding tax on interest** – Interests on current accounts and deposit accounts with banks, as well as bonds and similar securities, received by people resident in Italy for tax purposes is subject to a withholding tax of 20%, generally applied on account (gross interest is included in taxable income and the withholding is deducted from the gross tax). However, whereby the interest is received by residents outside the scope of a business activity, the withholding tax is applied in settlement and interest is not part of the overall taxable income.

Interests on current and deposit accounts, as well as bonds and similar securities, received by non-residents is not subject to any withholding tax, with the exception of persons resident in tax havens, for whom a 20% withholding tax applies.

In compliance with the EU Interest and Royalties Directive, withholding tax is not due on interest paid by companies resident in Italy for tax purposes or by permanent establishments in Italy of companies resident in the European Union to (i) resident companies, or (ii) permanent establishments of companies resident in other Member States of the European Union. In accordance with the Directive, the benefit is applicable if requirements concerning minimum holdings are fully met.

**Withholding Tax on Royalties** - In principle, interest from bank accounts and deposits, certain bonds, and similar securities are subject to

withholding tax at rates of 27% or 12.5%. These taxes, if any, on interest received by Italian residents generally consist of an advanced payment of income tax due by the recipients. As such, gross interest must be included in the recipient's tax base and the withholding tax deducted from the aggregate taxable income.

If non-Italian residents receive interest from bank accounts and deposits through an Italian permanent establishment, no withholding tax is due.

Interest and other profits from certain bonds issued by the state, by banks and by Italian-listed corporations are subject to a 12.5% substitute tax.

If Italian resident corporations receive interest from such bonds no substitute tax is due. If residents in countries listed in the so-called 'White List', e.g. those with adequate exchanges of information with the Italian tax authorities, receive interest from such bonds, not through an Italian permanent establishment, no substitute tax is due.

In principle, interest from loans received by residents other than business entities is subject to a 12.5% advance withholding tax. If non-residents receive interest from loans, not through an Italian permanent establishment, the withholding tax is a final payment of tax. The withholding tax rate is set at 27% for recipients resident in countries listed in the so-called 'Black List', ie, countries granting privileged tax regimes.

The withholding tax rate may be reduced under any tax treaties Italy has concluded with various foreign countries.

In line with the provisions of the EU Directive on Interest and Royalties, the withholding tax on interest payments is not levied if these payments are made by Italian resident companies or by Italian permanent establishments of EU resident companies to affiliated (i) companies resident, for tax purposes, in another EU Member State or to (ii) permanent establishments of companies resident, for tax purposes, in another EU Member State. In line with the above-mentioned

Directive, the benefit is applicable if certain shareholding requirements are satisfied.

**[C] Withholding tax on royalties** – Royalties paid to Italian resident corporations, or to Italian permanent establishments of non-resident corporations, are not subject to withholding tax. In principle, royalty payments to non-Italian residents are subject to a 30% final withholding tax. Under certain conditions, the tax base may receive a 25% flat deduction.

The withholding tax rate, if due, can be reduced under any tax treaties Italy has concluded with various foreign countries.

In line with the provisions of the EU Directive on Interest and Royalties, the withholding tax on royalty payments is not levied if these payments are made by Italian resident companies or by Italian permanent establishments of EU resident companies to (i) companies resident, for tax purposes, in another EU Member State or to (ii) permanent establishments of companies resident, for tax purposes, in another EU Member State. In line with the above-mentioned Directive the benefit is applicable if certain shareholding requirements are satisfied.

#### § 2.4 Tax treaties

In order to avoid double taxation, Italy has concluded tax treaties with the following Countries:

Albania	Georgia	Mexico	Sweden
Algeria	Germany	Morocco	Switzerland
Argentina	Greece	Mozambique	Tanzania
Australia	Hungary	New Zealand	Thailand
Austria	India	Norway	The Netherlands
Bangladesh	Indonesia	Oman	Trinidad & Tobago
Belgium	Ireland	Pakistan	Tunisia

<sup>5</sup> EU Directive No. 435/90.

Brazil	Israel	Philippines	Turkey
Bulgaria	Ivory Coast	Poland	Ukraine
Canada	Japan	Portugal	United Arab Emirates
China	Jugoslavia	Romania	United Kingdom
Cyprus	Kazakhstan	Russia	U.S.A.
Czechoslovakia	Kuwait	Senegal	Uzbekistan
Denmark	Lithuania	Singapore	Venezuela
Ecuador	Luxembourg	South Africa	Vietnam
Egypt	Macedonia	South Korea	Zambia
Estonia	Malaysia	Soviet Union	
Finland	Malta	Spain	
France	Mauritius	Sri Lanka	

The treaties generally provide more favourable tax treatment of Italian non-residents than the treatment provided under local Italian law.

Most of these treaties are based on the OECD Model Convention.

#### § 2.5 EU Parent-Subsidiary Directive

Italy has fully implemented the EU Parent-Subsidiary Directive for the abolition of double taxation on corporate profits generated by an EU subsidiary, and distributed to an EU parent resident in another EU Member State.<sup>5</sup>

According to the rules on taxation of dividends, dividends received by Italian parent corporations are 95% exempt from IRES regardless of the size of the underlying shareholding, and of the relevant holding period.

Dividends paid by Italian subsidiaries are exempt from withholding tax provided that the EU parent corporations hold, for an interruptive period of one year, a direct shareholding of at least 25% in the Italian subsidiaries. Italy has not yet implemented the Directive 123/2003 regarding, amongst the other, the reduction of the relevant threshold to 20%.

## § 2.6 EU Merger Directive

Italy has fully implemented the EU Merger Directive regarding the tax ramifications arising from mergers, divisions, transfers of assets and exchange of shares between EU-resident corporations.<sup>6</sup>

In line with the EU Merger Directive, Italian tax law specifies the conditions under which income, profits and capital gains from the above indicated business reorganizations - occurring between Italian and other EU-resident corporations - are deferrable.

## § 2.7 EU Directive on Interest and Royalty Payments

The EU Directive on Interest and Royalty Payments authorize provides for the abolishment of withholding tax on payments of certain interest and royalties between corporations resident in different EU Member States.<sup>7</sup>

The benefit of the exemption from withholding tax on payments made in favour of EU beneficiaries is subject, amongst the others, to the following conditions:

[A] The recipient is the beneficial owner of the interest and royalties payments. To this end, the recipient is regarded as the beneficial owner only if it receives the payment for its own benefit and not as an intermediary, such as an agent, trustee or authorised signatory, for some other person

[B] The interest and royalties payments are made:

[1] By a company which directly holds at least 25 per cent of the voting rights in the ordinary shareholders meeting (“Voting Rights”) of the company which receives the payment

[2] To a company which directly holds at least 25 per cent of the Voting Rights in the company which makes the payments

[3] To a company whose Voting Rights are directly held for a percentage not less than 25 per cent by a third company which also directly holds said minimum percentage in the company which makes the payments and in the company which receives the payments.

[C] The minimum 25 per cent stake at point (ii) above is held without interruptions for at least 12 months.

For the purposes of the exemption, the beneficial owner of the payments shall have to attest its residence through a certificate issued by the Tax Authorities of its State of residency.

The implementing Decree provides that the exemption is applicable on interest accrued or royalties payable as from January 1, 2004.

In addition, the Legislative Decree introduces a withholding tax of 30% on payments made to non-Italian residents deriving from licences of industrial, commercial and scientific equipments.

## § 2.8 Repatriation procedures and restrictions

Capitals, dividends, interests and royalties are freely transferable to and from Italy, and foreign citizens and business concerns are not subject to any restrictions on their repatriation. Transfers exceeding € 10,329.14 must however be notified to the Italian Foreign Exchange Office in accordance with the statutory regulations on money laundering.

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<sup>6</sup> EU Directive No. 434/90.

<sup>7</sup> EU Directive No. 434/03. See also the implementing Legislative Decree No. 143/05.