

Italy

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1.0 OVERVIEW

Italy imposes corporate and personal income tax on its residents on their worldwide income. Corporate income tax (IRES, in its Italian acronym) is imposed under Presidential Decree 917 of December 22, 1986 (also known as the income tax code, or ITC). Non-residents who carry on business in Italy and generate business income therein are subject to corporate income tax in Italy only on Italian income. In addition to the corporate income tax, the regional tax on productive activities (IRAP) is levied at a general 3.9% tax rate. Regional authorities may increase or decrease these rates to 0.92% on companies, partnerships and individuals that carry on activity aimed at the manufacturing or trading of goods and the supplying of services. Non-resident companies are also subject to IRAP provided that they maintain a permanent establishment in Italy for at least three months.

Dividends, interest and royalties paid by resident companies to non-resident companies without a permanent establishment in Italy are normally subject to a final outbound withholding tax. The amount of withholding tax can be reduced, or in some cases, eliminated under relevant treaty provisions or under the relevant EU directive(s), in the case the non-resident recipient is resident in another EU country.

Italy is a signatory to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI).

2.0 LEGAL SYSTEM

The Italian legal system takes the form of continental civil law. The basic rules governing commercial relationship are embodied in the Italian Civil Code, which was enacted in 1942, and superseded in other special laws or statutes. As a result of Italy's membership in the EU and of a number of EU directives, many parts of the Civil Code have been substantially modified over time. While as a general rule the ability to make laws are in the exclusive domain of the central state, there are some specific fields where the state and regions have overlapping jurisdiction.

3.0 TAXATION AUTHORITIES

The Italian tax system in Italy is administered by the Italian Revenue Agency (*Agenzia delle Entrate*). The agency is mainly responsible for collecting tax revenues, providing services and assistance to taxpayers and carrying out assessments and inspections aimed at countering tax evasion.

4.0 BUSINESS VEHICLES

Investments made in Italy by nationals of other EU member states are treated in the same manner as investments made by Italian nationals. Investments made by non-EU nationals may be subject to certain restrictions. Non-EU nationals may participate in Italian entities on the basis of reciprocity. A non-resident may either establish an Italian business vehicle to carry on business in Italy or operate directly through a foreign entity (with or without an Italian permanent establishment).

Italian law makes a clear distinction between partnerships, which include general partnerships and limited partnerships, and companies, which include joint-stock companies, limited liability companies and partnerships limited by shares.

4.1 Partnerships

Partnerships do not have a separate legal personality and as a result, partners are subject to unlimited liability, with the exception of the limited partners of a limited partnership. As a general rule, however, creditors' claims must be first enforced against the assets of the partnership before invoking the liability of the partners.

A partnership (whether general or limited) is generally treated as fiscally transparent for Italian income tax purposes and is not subject to IRES tax but only to IRAP tax. Taxable income is computed in the hands of the partnership, which must keep its own books and accounts and submit its own tax return. However, income is taxed in the hands of the partners in proportion to their entitlement of the partnership's profits, even if it is not distributed out as dividends.

Much like the income of companies subject to IRES, the income of a partnership 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 contribution. The income of an Italian partnership that is allocated to non-resident partners

is taxed at a rate of 24% and is always taxed in Italy as business income, even if the non-resident partner has no permanent establishment in Italy.

4.2 Corporations

Joint-stock companies and limited liability companies are considered legal persons; consequently, their shareholders are not personally liable for company debts. The establishment of a corporation requires a minimum capital requirement equal to €50,000 for a joint-stock company (of which at least 25% must be paid upon the incorporation) and to €10,000 for a limited liability company (of which at least 25% must be paid upon the incorporation).

A partnership limited by shares, however, has two categories of shareholders. General partners are vested with the management of the company and are jointly and severally liable without limitation for the company's obligations. Limited partners are liable only for an amount equal to the capital to which they subscribed.

4.3 Foreign corporation (with or without an Italian branch)

A foreign corporation that carries on business in Italy is subject to tax under the ITC in respect to the income derived from Italy. Where the foreign corporation is resident in a country with which Italy has a double taxation treaty, the corporation may claim treaty benefits and will generally be exempt from Italian tax on its business profits except to the extent that the profits were earned through a permanent establishment in Italy.

A foreign company may establish a branch to perform business activity in Italy. The branch is not considered a legally separate entity from its parent company. Its establishment must be registered with the Register of Companies. A branch is subject to fewer statutory obligations regarding a company's requirements.

From a tax point of view, a branch is in principle deemed a permanent establishment of the foreign company and it is treated as an independent entity. In general, a branch is subject to the same tax treatment as an Italian company and is subject to corporate taxes for profits produced in Italy. The branch must draw up yearly financial registers. It is subject to the same tax commitments as Italian companies, including keeping official registers, and it is obligated to pay corporate taxes as well as file VAT returns.



5.0 FINANCING A CORPORATE SUBSIDIARY

Italian companies are free to finance investments through debt financing, equity financing or a mixture of both.

5.1 Equity financing

5.1.1 Contributions of equity

Contributions of equity can occur by way of new capital injections or through conversion of existing equity reserves, including those composed of retained earnings. Capital can also be increased by contributing assets in kind. Apart from capital increases, the grant from shareholders or quota holders is one of the most commonly used means through which a company may increase its financial capability. For tax purposes, cash contribution as a means of equity financing increases the shareholder's cost base.

5.1.2 Reduction of equity

As a general rule, capital reserves that are distributed are not taxable as dividends. Rather, they reduce the cost base of the shares; once the cost base is zero, any excess becomes taxable as a dividend outside business income, or as a capital gain within a business income framework. However, there is a presumption that any profit reserves available for distribution are deemed to be distributed before capital reserves, irrespective of the shareholders' meeting resolution and the reserves deemed to be distributed based on the relevant resolution wording.

Capital distributions work similarly. Ordinarily they are not taxable as dividends, but reduce the cost base of the shares. However, to the extent that profit reserves were previously imputed to capital, they

take precedent in any distribution, which is correspondingly taxable as a dividend.

5.1.3 Stamp tax

A €200 fixed registration tax applies on a capital increase and a reduction of the statutory equity paid in cash.

5.2 Debt financing

5.2.1 Withholding tax implications

Italian companies are subject to IRES at a rate of 24% on interest income. Non-financial companies are not subject to IRAP on interest income, while banks, financial institutions and insurance companies are.

Italian-source interest paid to a non-resident is generally subject to a 26% withholding tax (WHT), and interest is considered as sourced in Italy whenever paid by an Italian resident. The 26% WHT is usually operated and paid by the borrower, in its capacity as the person paying the interest and being qualified as withholding agent. No WHT applies to interest due on medium- and long-term financing granted by EU banks, insurance companies and white-listed institutional investors, provided that no regulatory constraints are breached.

If all the requirements requested by the EU Interest and Royalties Directive are met, interest paid to an EU corporate entity is free from WHT. Provided the relevant conditions set forth therein are met, some double taxation treaties may foresee a reduction of the outbound withholding taxation. Interest expenses incurred by Italian resident companies on loans borrowed from non-resident related

parties must be set at arm's length, meaning a comparable loan would have been entered into between unrelated parties.

5.2.2 Thin capitalization

If an Italian subsidiary is to be financed with debt, it may be subject to the thin capitalization rules contained in the ITC. Italy has adopted an EBITDA earnings stripping rule under which interest expenses (net of interest income) are deductible up to 30% of the EBITDA produced by the company in the same fiscal year. The amount of financing cost exceeding 30% of the EBITDA is not deductible from the taxable income of the relevant fiscal year, but may be carried forward to a subsequent fiscal year, without any time limitation. As from 2019, the EBITDA is calculated taking into account the adjustments provided by Italian tax law.

5.2.3 Stamp tax or similar tax

Financing transactions such as loans may fall within the scope of value-added tax (VAT), although exempted. If not subject to VAT (e.g., because the lender is not a VAT subject), they are subject to registration tax at 3%, unless they are executed by exchange of correspondence, which is one of the means to conclude a legal contract, requiring fewer formalities. In these cases, guarantees are provided, which may trigger additional registration taxes, as well as mortgage and cadastral taxes if real estate is involved.

However, medium- to long-term loans (defined as exceeding 18 months) granted from banks and other qualified financial institutions may benefit from the application of

an optional substitute tax generally levied at a rate of 0.25% of the total amount of the loan requested, instead of the levying of stamp duty, government license tax and registration, and mortgage and cadastral taxes.

6.0 CORPORATE INCOME TAX

6.1 Income tax rate

In 2018, the IRES is 24%. The taxable base is the worldwide income shown in the profit and loss account prepared for the relevant financial year according to company law rules and adjusted according to tax law provisions. The tax basis can be reduced through multiple deductions provided by tax law provisions.

In addition to IRES, the IRAP is levied at a general rate of 3.9% (whereby regional authorities may decrease or increase these rates up to a maximum of 0.92% in either direction) on companies, partnerships and individuals that carry on an activities related to the manufacturing and trading of goods, or the supplying of services.

6.2 Capital gains

As a general rule, gains from the disposal of capital assets is computed as the difference between (i) the sale price or the indemnity received, reduced by the costs directly attributable to the sale or the indemnity, and (ii) the asset's adjusted tax basis. The difference is included in taxable income for the fiscal year during which these gains are realized. If the property being sold has been held for at least three years, capital gains may be included, at the company's option, in its entirety for the year in which they are realized, or in equal installments

for the current and following tax years, but not carried beyond the fourth year.

Special rules apply to capital gains from the alienation of shares, financial instruments assimilated to shares and interests in resident companies or partnerships that are exempt from tax for 95%. This "participation exemption" regime—duly coordinated with the EU fiscal framework on the matter—grants a 95% exemption to the capital gain arising from the sale of the financial instruments in question. The exemption applies, provided that (i) the participation has been held at least from the first day of the twelfth month preceding the alienation, (ii) the participation is classified as a financial asset in the first balance sheet closed after the acquisition and (iii) the participating company has been engaged in an active trade or business since at least the beginning of the third financial year preceding the alienation. An active trade or business would mean that a company has an operational structure suitable for manufacturing or sales activity in connection with goods or services that potentially generate revenue.

Non-resident companies that have a permanent establishment in Italy are taxed on the gains realized on assets pertaining to their business activity in Italy. For non-resident companies without a permanent establishment in Italy, the taxation of capital gains depends on the kind of property that is disposed of:

- i. Real estate property situated in Italy is taxable as miscellaneous income in Italy if the asset is situated in Italy. These gains are not subject to tax if the

transferor has held the property for more than five years

- ii. Movable assets are taxed in Italy if the assets are in Italy, unless a tax treaty prevents the taxation of the gain
- iii. Shares of a corporation that give rise to capital gains from the sale of participating interests are subject to taxation in Italy only if the participation is in an Italian company.

In the case of participations in publicly listed companies, if the amount of participation sold during a 12-month period does not exceed 2% of the voting rights, or 5% of the capital, the capital gain is not regarded as Italian-source income and not subject to taxation in Italy.

In the case of participation in non-listed companies, if the amount of participation sold during a 12-month period does not exceed 20% of the voting rights, or 25% of the capital, the capital gains are subject to a 26% substitute tax. This is referred to as "non-qualified participations." However, such capital gains are not subject to taxation if the seller is a resident of a country that Italy has an adequate exchange-of-information system with. A white-list of the states and territories that have an adequate exchange-of-information system has been issued by a ministerial decree.

If the size of the participation sold during a 12-month period exceeds 2% of voting rights (or 5% of capital, in the case of participations in listed

companies) or 20% of voting rights (or 25% of capital, in the case of other participations), the capital gain realized as from January 1, 2019, will be as well subject to 26% substitute tax.

Generally, consideration must be given to a double taxation treaty between Italy and the transferor's country of residence, containing a provision similar to Article 13 of the Organisation for Economic Co-operation and Development (OECD) Model Convention, which prevents capital gains on the sale of movable property from being taxed in Italy. Some specific treaties entered into by Italy (such as that with France) do foresee specific exceptions to the exemption rule under certain conditions.

6.3 Branch tax

No branch profits tax or similar tax is levied in Italy on branches of non-resident companies.

6.4 Computation of taxable income

6.4.1 Taxable base

A taxpayer is subject to tax on its profits from carrying on business. The taxable base is the worldwide income shown on the profit and loss account prepared for the relevant fiscal year according to company law rules and adjusted according to the tax law provisions concerning business income.

6.4.2 Deductions

A taxpayer is generally permitted to deduct its current expenses in computing business income. As a general rule, costs and expenses may be deducted only if they are incurred for the production of income. This rule does not apply to certain

deductible items, such as interest, which is subject to a special rule.

6.5 Income tax reporting and payment of tax obligations

Italian resident corporations and non-resident corporations that carry on business in Italy or that dispose of taxable Italian real estate property are required to file an annual corporate income tax return in Italy. Corporate tax returns must be filed electronically through an authorized intermediary by (i) October 31 of the following year, if the company adopts the calendar year as fiscal year, or (ii) within nine months of the end of the fiscal year.

Corporate income tax is normally paid as follows:

- i. A first advance payment of the IRES due for the current fiscal year must be paid at the same time as the balance due for the previous fiscal year (i.e., the last day of the sixth month following the end of the previous year) and is equal to 40% of the tax due for the previous fiscal year
- ii. A second advance payment of the IRES due for the current fiscal year must be paid by the last day of the eleventh month following the end of the previous fiscal year and is equal to 60% of the tax due for the previous fiscal year
- iii. The balance must be paid by the last day of the sixth month following the end of the fiscal year.

7.0 CROSS-BORDER PAYMENTS

7.1 Transfer pricing

Italian's transfer pricing regime generally conforms to the arm's length principle of the OECD.

The ITC permits the Agenzia delle Entrate to impose a transfer pricing adjustment in respect of a transaction that was not made on arm's length terms or conditions.

Italian taxpayers are also required to keep and be prepared to provide transfer pricing documentation evidencing how the transfer prices were set. The documentation must comply with certain formal and content requirements set forth by the tax authorities (Commissioner's Regulation 137654/2010). If during the transfer pricing audit, the taxpayer provides duly kept and prepared transfer pricing documentation, no penalty will be charged even in the case of transfer pricing adjustments.

On the other hand, if the taxpayer fails to keep adequate documentation, it is liable for a penalty that can range from 100% to 200% of the tax due on the adjustment, in addition to the tax due.

7.2 Withholding tax on passive income

Payments made by Italian resident entities to a non-resident in respect of interest payments, royalties and dividends are subject to tax in Italy. The following items of income are subject to a final WHT at the rates specified below.

- i. **Dividends** are generally subject to a 26% WHT. If the recipient can provide evidence through documentation issued by the tax authorities of its country of residence that it has paid a final tax on the same dividends, the recipient may be refunded up for a percentage equal to 11/26 of the initial amount of the

withholding tax. A reduced WHT rate of 1.2% is levied on dividends if the beneficial owner is a company resident and subject to corporate income tax in another EU or European Economic Area country that allows an adequate exchange of information with Italy. In addition, WHT may be reduced or exempted pursuant to the application of the tax treaty in force between the Italy and the country of residence of the recipient. If all the requirements provided for by EU Parent-Subsidiary Directive are met, no withholding tax is levied on the outbound flow of dividends

- ii. **Interest income** paid to non-resident persons is subject to a WHT rate of 26%, or 12.5% on interest from government bonds and bonds issued by certain project finance companies (project bonds). If all the requirements provided for by EU Interest-Royalties Directive are met, no withholding tax is levied on the outbound flow of interests. No withholding tax applies with reference to interest due on medium- and long-term financing granted by EU banks, insurance companies and white-listed institutional investors
- iii. **Royalties** paid to non-resident companies are subject to a 30% WHT, which is generally applied to 75% of the gross amount of the payment, resulting in an effective rate of 22.5%. If all the requirement provided for by EU Interest-Royalties are met, no WHT is levied on the outbound flow of royalties.

8.0 PAYROLL TAXES

8.1 Payroll tax

No payroll taxes are imposed on corporate taxpayers.

8.2 Social security contributions

A complicated system of social insurance covering life insurance, health, maternity, disability, unemployment and family allowances is in operation for all employees.

The amount of social security contributions depends on the type and size of the business and the rank of the employee. The aggregate contributions range from approximately 40% to approximately 45% of the aggregate remuneration accrued in the relevant year.

The aggregate contributions are normally borne by the employer for 80% to 85% of their amount. The remainder is borne by the employee and must be withheld directly by the employer. Social security contributions payable by employers are deductible for corporate income tax purposes.

9.0 INDIRECT TAXES

9.1 Value-added tax (VAT)

VAT is levied at all levels of the supply of goods and services that takes place in Italy and on acquisitions from other EU member states. VAT is also levied on the importation of goods from outside the EU. The general VAT rate is 22%. Reduced rates of 10%, 5% and 4% apply in certain specific circumstances. VAT is not imposed on all the financial services, insurance and reinsurance, activities related to shares, bonds and other securities and medical services.

VAT is due by all persons, irrespective of their residence, that make taxable supplies in Italy. Non-residents that have no permanent establishment in Italy may appoint a representative to exercise their rights and fulfil their obligation under the VAT law. Residents of other EU member states may directly exercise their rights and fulfil their obligations in Italy. Non-residents must provide a declaration to the competent authority containing certain information to receive a VAT number before executing any taxable transactions in Italy. This regime extends to residents of non-EU states with which Italy has concluded an agreement on mutual assistance in respect of indirect taxes.

9.2 Financial transactions tax

A financial transactions tax (FTT) is levied on transfers of ownership of shares and certain participating financial instruments issued by companies that have their registered office in Italy, regardless of the place of residence of the parties involved and of the place where the contract has been executed.

The FTT is due by the person to whom the ownership of the shares is transferred (the transferee). The standard FTT rate is 0.20% for over-the-counter transactions, which is reduced to 0.1% for transactions executed on regulated markets, a multilateral trading facility established in an EU member state or, subject to certain conditions, in a country included in the white list. Several exemptions and exclusions apply to some specific transfers and financial operations.

9.3 Transfer tax on immovable property

A registration tax is levied on the transfer of immovable property located in Italy. The rates vary according to the property transferred. The standard rate is 9%; a 15% rate applies on transfers of agricultural land, except for transfers to agricultural entrepreneurs. In all cases, the minimum registration tax levied is €1,000. The transfer of land suitable for building (terreno edificabile)

is subject to VAT at 22% and registration tax at the lump sum of €200 (plus mortgage and cadastral taxes). Indirect taxes (VAT, registration tax, mortgage and cadastral taxes) application on immovable properties (other than lands) depends on the nature of the immovable property (commercial or residential properties) and the nature of the seller as the below table sums up.

Properties	Seller	VAT	Registration tax	Mortgage and cadastral taxes
Commercial properties	Construction companies that built or restored the properties within 5 years before the sale	22% (or 10% in certain cases)	€ 200	3% + 1%
	Construction companies that built or restored the properties after 5 years from the sale and other VAT-taxable persons	Exempt or option for VAT application through reverse-charge mechanism (22% or 10% in certain cases)	€200	3% + 1%
	Non VAT-taxable persons	Out of scope	9% (minimum €1,000)	€50 + €50
Residential properties	Construction companies that built or restored the properties within 5 years before the sale	10% (4% for first house; 22% for luxury house)	€200	€200 + €200
	Construction companies that built or restored the properties after 5 years from the sale that opted for VAT application	VAT application through reverse-charge mechanism (10% or 4% for first house or 22% for luxury house)	€200	€200 + €200
	Construction companies that built or restored the properties after 5 years the sale that did not opt for VAT application and other VAT-taxable persons	VAT exemption	9% (2% for first house) (minimum €1,000)	€50 + €50
	Non VAT-taxable persons	Out of scope	9% (2% for first house) (minimum €1,000)	€50 + €50

9.4 Registration tax

In general, a registration tax is due on contributions of cash and assets in exchange of shares. In the case of cash contributions and contributions of assets other than immovable property, the tax is levied as a lump sum of €200. The registration tax on contributions of immovable property varies depending on the type of property and the nature of the contributor. Please refer to the above table for information on the indirect

tax regime of immovable properties (other than lands) including mortgage and cadastral taxes.

9.5 Stamp duty

Stamp duties are levied on certain documents, contracts and registers. The tax is usually a nominal lump sum, but in some specific cases, such as bills of exchange, it is levied as a percentage of the value mentioned in the document.