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Corporate Tax

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During 2016 there has been a considerable intensification of M&A deals in Italy.

The M&A market in Italy has been stimulated by both domestic and cross-border transactions.

The Italian M&A market in the first six months of 2016 saw 298 deals worth a total of €25.3bn, up 47% from €17.2bn in the same period the year before.

Data confirmed the interest of foreign investments in Italy: in the first six months of the year, there were 105 transactions worth a total of €6.7 billion. The biggest included the acquisitions of Italcementi by Heidelberg for €3.7bn and that of Rhiag by Lkq for €1bn.

Over the last year, the Italian M&A market has also registered a substantial development in special purpose acquisition companies.

The main factors impacting deal structures in 2016 have been costs, timing and tax changes.

Corporate tax work focused primarily on the tax aspects of corporate acquisitions.

Below is a short summary of last year's relevant transactions where tax structuring has played a very important role.

Transfer pricing: remains a remarkably important driver in all cross-border transactions. The tax provisions in Law Decree of April 24, 2017, No. 50 include a number of measures relating to transfer pricing, which generally are designed to align Italian regulation more closely with the standards set out by the Organisation for Economic Co-operation and Development (OECD).

Real estate: the real estate market is undergoing a phase of improvement in Italy and there are indications of an increase in transactions in line with the average in the four other major European countries for the coming two years, according to the research institute Scenari Immobiliari.

Looking at the sector breakdown, the residential segment saw an increase in sales to 510,000 deals in 2016, up 14.6% compared to the year before. Revenues in this segment totalled €85.1bn in 2016, an annual increase of 2.5%.

Luxury and Fashion: with revenues of approximately €84bn, Italy has the most active fashion and luxury industry in the world, and without a doubt, represents one of the most economically influential sectors of the Italian economy.

Entertainment/Gaming: Tax revenues collected by the Italian government from the online gambling industry have increased, reaching €247m, up 21% compared to 2015. In 2015, the Italian government collected €205m from online betting.

Key developments affecting corporate tax law and practice

During 2016 and 2017, many measures have significantly changed the Italian tax system.

A Circular Letter (no. 6/E/2016) issued by the Italian tax authorities provided detailed guidelines on the tax ramifications of leveraged buy-out (LBO) acquisitions. The newly published guidelines provide important clarifications concerning the deductibility for corporate income tax purposes of the interest expenses borne in connection with acquisition loans and the appropriate tax treatment of certain items of income paid by target companies and their Special Purpose Vehicles (SPV).

A summary of some key points addressed by the Inland Revenue Agency in the Circular is provided below.

Deductibility of interest expenses: according to the new approach outlined by the Circular, the Italian acquisition vehicle may deduct interest expenses and, if at arm's length, it does not have to be charged to the shareholder.

Tax treatment of other selected items of income: the second part of the Circular addresses a number of different and selected tax issues potentially arising in LBO transactions, even though it should be observed that many of the clarifications provided by these administrative guidelines might also have an impact on transactions in other areas.

The new guidelines indicate that the corporate income tax treatment of transaction fees and of similar fees charged by investment managers and other entities or advisors connected with the private equity firm should be duly scrutinised on a case-by-case basis, with respect to their deductibility under general tax principles.

On 7 December 2016, the Italian Parliament approved the budget law for year 2017.

Most relevant tax measures contained in the law relate to:

Corporate tax rate provisions: with effect from fiscal year 2017, the budget law for 2016 has decreased the corporate tax rate of 3.5% and provided a 3.5% surcharge for banks and financial entities for which, thus, the overall corporate tax rate will remain unchanged.

Group VAT: the law introduces the option for European Group VAT, starting from 1 January 2018 (as provided by Art. 11 of EU Directive 2006/112/CE in the Italian VAT law).

Group VAT allows the treatment of Italian-based companies as a single VAT taxpayer, provided that at least from 1 July of the previous year, the following requirements are met:

- Direct or indirect control relationships between entities must be controlled directly or indirectly by the same entity in that group, provided that it is resident in Italy or in a State having exchange of information with Italy.
- The entities must all perform a business activity of the same nature or, alternatively, a complementary activity or an activity that supports one or more entities of the group.
- There must be coordination, in accordance with the Italian Civil Code, between the management bodies of the same entities, even if carried out by a third entity.

Extension of extra-amortisation of certain tangible and intangible assets: the law extends the 40% extra-amortisation rate introduced by the budget law for 2016 in relation to the purchase of tangible assets for which the amortisation rate for tax purposes exceeds 6.5%.

The Italian budget law also introduced an "anti-avoidance" rule under paragraph 6-*bis*, Art. 1 of the Italian Law Decree 201/2011.

Also important is the below summary of the most important changes introduced by **Law Decree 22 October 2016, no. 193, converted into Law 1 December 2016, no. 225** (published in the Official Gazette on 2 December 2016, no. 282).

Integrative tax return "in favour" of taxpayers

The possibility to file an integrative tax return in favour of taxpayers within the deadlines for tax assessment has been introduced.

Option for special tax regimes

From FY 2017 onwards, automatic renewal for the special regimes provided by the Italian tax rules of: fiscal transparency; domestic tax consolidation; and worldwide tax consolidation, are applicable.

Settlement of tax bills

The possibility to settle tax bills issued for financial years 2000–2016 has been granted by the tax collection agents without reimbursement of the relevant penalties and interests for late payment.

In the current year, the Italian Government adopted **Law Decree 24 April 2017, no. 50** which introduces several tax measures aimed at boosting economic development and stabilising State revenues.

Law Decree no. 50 of 24 April 2017(1) was converted into law on 15 June 2017.

The most important measures in this law relate to:

- a measure replacing the concept of fair market value with an arm's length concept for transfer pricing purposes; and
- a tax ruling procedure whereby multinational entities can apply to the Italian Tax Agency in order to obtain a decision about whether their business activity constitutes a permanent establishment in Italy.

Tax climate in Italy

In 2016, Italy launched a particularly ambitious project for the renovation of its tax administration in terms of organisation and function.

Italy has the world's most complex tax system, according to the first annual Financial Complexity Index compiled by TMF Group in a ranking of 94 jurisdictions worldwide.

The Italian Revenue Agency has taken steps in the last few years to simplify the tax system, introducing a cooperative compliance program that helps companies obtain opinions on their tax treatment ahead of making investments.

One of the principal problems that still affects the Italian tax system is that taxation is levied at national, regional and municipal levels, and taxpayers have to pay a high number of taxes.

Developments affecting attractiveness of Italy for holding companies

The Italian economy has made a strong step forward during the last year, as many companies have increased their output.

External demand has also risen, which is one of the main reasons that Italy has started to attract more foreign investors. Most of such investors decide to set up holding companies in Italy, as it is one of the most advantageous ways of running a business in the country.

The participation exemption provides for a 95% tax exemption for dividends paid by the Italian subsidiary to its foreign shareholders, such as the holding company. In Italy there is no minimum period for qualifying for the participation exemption.

Industry sector focus

Banking

In spite of the lengthy recession, the Italian banking system is solid and has demonstrated a good capacity for resilience; it has managed to resist difficulties and adapt to changes.

Despite the solidity of the banking sector as a whole, there still remain some of the historical limits to the Italian banking sector, such as the excessive fragmentation of supply, the limited availability of types of financing diverse from bank credit, and the disproportionately long times for recovering NPLs.

Corporate real estate

A new window has been opened for Italian companies to benefit from a tax-simplified method of transferring certain assets (real estate and registered movable property) to their shareholders/partners in the case of a contribution or disposal or transformation into a simple partnership, which is open until 30 September 2017. The tax regime will be available for both "dormant" and "non-dormant" companies; an 8% substitute tax (10.5% in the case of dormant companies) will be applied to the difference between the cost recognised for tax purposes and the fair market value of the assets. Any deferred tax reserve eliminated as a result of the relevant transactions will be subject to a 13% substitute tax. Registration tax, if due on the specific transaction, will be applied at 50% of the normal rates, while mortgage and cadastral taxes will be applied on a lump-sum basis.

The year ahead

During the year ahead, corporate tax reform will continue to be at the centre of attention.

The Italian tax system is undergoing substantial reforms towards harmonisation with the European system.

Further developments in the area of corporate taxation with a focus on transfer pricing are expected. Moreover, capacity building of the tax authority remains one of the crucial success factors of the modernisation of the Italian tax system.

A large number of M&A operations as well as an expected increase in transactions involving NPLs will continue to characterise 2017.

BEPS and tax avoidance will continue to gain the attention of both the tax administration and tax advisors, also considering the parallel developments at the EU level, including legislative measures on transparency and exchange of information, as well as covering financial information and APAs.

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He taught International Taxation at the Master's Course on International and European Taxation of the University of Palermo. He also taught Taxation and Public Finance at the Faculty of Economics of the University of Palermo.
He has been appointed as a member of the board of contributors of "*Diritto e pratica tributaria internazionale*", the most important Italian review specialising in international taxation.
His publications include several articles on national and international taxation topics and a book, "*Potestà normativa ed agevolazioni fiscali*", published in 2008.
He has been appointed as an advisor for taxation matters to the President of the Sicilian Parliament and to the Councillor for Finance of the Sicilian Region.
He is an active member of the Aspen Institute Italia. He is the Vice President of ANTI (*Associazione Nazionale Tributaristi Italiani*) – Western Sicily chapter.
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