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## **CORPORATE TAX ITALY**

### **A. At a Glance**

Corporate Income Tax Rate (%)	27.5	(a)
Capital Gains Tax Rate (%)	0/27.5	(b)
Branch Tax Rate (%)	27.5	(a)
Withholding Tax (%)		
Dividends	0/12.5/27	(c)(d)
Interest	0/12.5/27	(e)(f)
Royalties from Patents, Know-how, etc.	22.5/30	(g)
Branch Remittance Tax	0	
Net Operating Losses (Years)		
Carry back	0	
Carry forward	5	(h)

(a) Under the 2008 Budget Law, the corporate income tax (*imposta sul reddito delle società*, or IRES) rate is reduced from 33% to 27.5%. A regional tax on productive activities (*imposta regionale sulle attività produttive*, or TRAP) is imposed on the net value of production. For further details regarding TRAP, see Section B.

(b) For details concerning capital gains taxation, see Section B.

(c) Withholding tax is not imposed on dividends paid to resident companies. The 12.5% rate applies to dividends paid to resident individuals with non-substantial participations (for information on substantial and non-substantial participations, see discussion of capital gains taxation in Section B). The 27% rate applies to dividends paid to nonresidents. Nonresidents may be able to obtain a refund of the withholding tax equal to the amount of foreign tax

paid on the dividends. However, the maximum refund is 4/9 of the withholding tax paid. Tax treaties may provide for a lower tax rate. Under the 2008 Budget Law, a 1.375% rate applies under certain circumstances (see Section B).

- (d) Under the European Union (EU) Parent-Subsidiary Directive, dividends distributed by an Italian subsidiary to an EU parent company are exempt from withholding tax, if among other conditions, the recipient holds 15% or more of the shares of the subsidiary for at least one year (the required ownership percentage will be reduced to 10%, effective from 2009). See Section B.
- (e) The 0% rate applies to interest derived by nonresidents on the white list (see Section B) from treasury bonds, bonds issued by banks and listed companies (if maturity is at least 18 months), nonbank current accounts and certain cash pooling arrangements. The 12.5% rate applies to interest derived by residents and nonresidents not on the white list from loans in general (including, in principle, cash pooling) and on treasury bonds and corporate bonds (if maturity is at least 18 months). In general, the 27% rate applies to interest paid on deposit certificates, bank accounts and corporate bonds (if maturity is less than 18 months). It also applies to loan interest paid to a recipient from a tax haven (a jurisdiction on the black-list). For resident individuals carrying on business activities in Italy and resident companies, the interest withholding taxes are advance payments of tax. For other resident individuals and nonresident individuals and companies, the interest withholding taxes are final taxes.
- (f) Effective from 1 January 2004, no withholding tax is imposed on interest and royalties paid between associated companies of different EU member states if certain conditions are met. For details, see Section B.
- (g) The withholding tax rate of 30% applies to royalties paid to nonresidents. However, in certain circumstances, the tax applies to 75% of the gross amount, resulting in an effective tax rate of 22.5%. These rates may be reduced under tax treaties.
- (h) Loss carry-forwards are allowed only for corporate income tax purposes. Losses incurred in the first three tax years of an activity may be carried forward indefinitely. Anti-abuse rules may limit loss carry-forwards.

## **B. Taxes on Corporate Income and Capital Gains**

**Corporate Income Tax.** Resident companies are subject to corporate income tax (*imposta sul reddito delle società*, or IRES; this tax was formerly known as *imposta sul reddito delle persone giuridiche*, or IRPEG) on their worldwide income. A resident company is a company that has any of the following located in Italy for the majority of the tax year:

- Its registered office;
- Its administrative office; or
- Its principal activity.

Unless they are able to prove the contrary, foreign entities controlling an Italian company are deemed to be resident for tax purposes in Italy if either of the following conditions is satisfied:

- The foreign entity is directly or indirectly controlled by Italian resident entities or individuals; or
- The majority of members of the board of directors managing the foreign entity are resident in Italy.

Nonresident companies are subject to IRES on their Italian-source income only.

### *Rate of Corporate Tax.*

Under the 2008 Budget Law, the IRES rate is reduced from 33% to 27.5%.

### *Local Income Tax.*

Resident and nonresident companies are subject to a regional tax on productive activities (*imposta regionale sulle attività produttive*, or TRAP) on their Italian-source income.

For manufacturing companies, TRAP is imposed at a rate of 4.25% on the net value of production, which is calculated by subtracting the cost of production from the value of production. An 8.5% rate applies to public entities performing commercial activities. Under the 2008 Budget Law, the TRAP rate is reduced to 3.9%.

Special rules for the calculation of the tax base for TRAP purposes also apply to banking institutions, insurance companies, public entities and noncommercial entities. Special rates may also apply. Each region may increase or decrease the rate of TRAP by a maximum of one percentage point. Companies generating income in more than one region are required in the TRAP tax return to allocate their tax base for TRAP purposes among the various regions and to pay the applicable tax to the local tax authorities. Under the 2008 Budget Law, the annual TRAP return must be filed with the regional tax administrations, separately from the annual IRES return, which continues to be filed with the central tax administration.

Certain deductions are not allowed for TRAP purposes, such as certain extraordinary costs, credit losses, labor costs (excluding certain compulsory social contributions), and interest expenses (except for banks, insurance companies and holding companies).

## **Capital Gains**

### *Resident Companies and Nonresident Companies with a Permanent Establishment in Italy.*

In general, capital gains derived by resident companies or nonresident companies with a permanent establishment in Italy are subject to IRES and TRAP. Gains derived from disposals of participations and extraordinary capital gains are excluded from the tax base for TRAP purposes. Extraordinary gains are gains not related to the core business of the company, such as those derived from transfers of going concerns.

Capital gains on assets that have been held for at least three years may be taxed, at the taxpayer's option, entirely in the year of sale or spread over a maximum period of five years.

Italian corporate taxpayers (that is, companies and branches) may benefit from an 84% participation exemption regime (that is, only 16% is taxable) for capital gains derived from disposals of Italian or foreign shareholdings that satisfy all of the following conditions:

- The shareholding is classified in the first financial statements closed during the holding period as a long-term financial investment.
- The Italian parent company holds the shareholding for an uninterrupted period of at least 18 months before the disposal.
- The subsidiary actually carries on a business activity (real estate companies can satisfy this requirement only under certain limited circumstances).
- The subsidiary is not resident in a tax haven (a jurisdiction on the black list). The 2008 Budget Law contains a measure that replaces the existing black list system with a white list contained in a ministerial decree to be issued after the enactment of the Budget Law. The primary criterion for inclusion on the white list is the effective exchange of information with the Italian tax authorities. Beginning with the third financial year (three full book years) before the year of the disposal, the last two conditions described above must be satisfied uninterruptedly.

Under the 2008 Budget Law, the participation exemption percentage increases to 95% for capital gains derived in fiscal years beginning on or after 1 January 2008. However, the 84% exemption continues to apply to capital gains realized up to the amount of devaluations deducted before the 2004 fiscal year.

If the conditions described above are not satisfied, capital gains on disposals of shares are fully included in the calculation of the tax base for TRES purposes. Capital gains on investments that have been recorded in the last three financial statements as fixed assets may be taxed over a maximum period of five years. In addition, any capital losses derived from disposals of such shareholdings may be deducted.

In principle, capital losses on shares are deductible. However, capital losses on participations that would benefit from the 84% participation exemption are 100% nondeductible (and a 12-month holding

period applies instead of an 18-month period). Losses from sales of participations not qualifying for the participation exemption are deductible for tax purposes only up to an amount equal to the taxable portion of the dividends received on participations. This rule applies to sales of participations acquired during the preceding 36 months.

*Nonresident Companies without a Permanent Establishment in Italy.*

If no treaty protection is available, capital gains derived from sales of shares in Italian companies and partnerships by nonresident companies are subject to tax in Italy. Only 40% of capital gains on shares qualifying as a “substantial participation” is included in taxable income for corporate income tax purposes and taxed at the standard rate of 33% (that is, a 13.2% effective tax rate). Because of the decrease of the IRES rate from 33% to 27.5% under the 2008 Budget Law, a ministerial decree will be issued to adjust the percentage of exemption for capital gains to the new corporate income tax burden.

A “substantial participation” in a company listed on a stock exchange requires more than 2% of the voting rights at ordinary shareholders’ meetings or 5% of the company’s capital. For an unlisted company, these percentages are increased to 20% and 25%, respectively.

Capital gains on “non-substantial participations” are subject to a substitute tax of 12.5%. However, certain exemptions may apply, such as for nonresident shareholders resident in white list jurisdictions.

### ***Administration***

Income tax returns must be filed by the end of the 7th month following the end of the company’s fiscal year. Companies must make advance payments of their corporate and local tax liability equal to a specified percentage of the tax paid for the preceding year.

*Tax Rulings*

Several tax ruling procedures are available in Italy.

Taxpayers may request ordinary tax rulings to clarify the application of tax measures to transactions if objective uncertainty exists regarding the tax law. The request for an ordinary tax ruling must include the identification data for the taxpayer, a description of the transaction and a list of applicable measures, circulars and court decisions.

Specific tax rulings are available with respect to a limited range of operations that could result in tax avoidance, including the following:

- Corporate reorganizations;
- Transactions subject to fictitious interposition legislation (legislation under which the tax authorities may attribute income to the beneficial owner);
- Deduction of advertisement and entertainment expenses;
- Exchanges of tax credits and excess taxes;
- Tax-haven transactions;
- International group companies; and
- Tax restrictions on non-operating companies.

In the event of litigation, the burden of proof is on the party that did not comply with the opinion. In practice, specific rulings are not binding on the tax authorities but they shift the burden of proof to them.

An international ruling scheme specifically deals with transfer pricing and cross-border interest, dividends, and royalties. An international ruling is binding for the fiscal year in which the ruling is entered into and for the following two fiscal years, unless material changes in legal or economic circumstances arise.

## ***Dividends***

A participation exemption regime applies to dividends. Under this regime, dividends distributed by companies to Italian entities subject to IRES (companies and branches) are 95% exempt from corporate taxation regardless of the source (domestic or foreign) of such dividends.

Italian parent companies are taxed on 100% of the dividends received from a subsidiary resident in a black-list (tax haven) jurisdiction, unless it obtains a ruling to the contrary from the Italian tax authorities. In addition, Italian parent companies receiving dividends from an intermediate holding company resident in a jurisdiction not on the black list are fully taxable on the dividends to the extent that these dividends derive from indirect subsidiaries resident in black list jurisdictions.

Under the 2008 Budget Law, the above mentioned black list is replaced by a white list provided by a ministerial decree. The following are the significant aspects of the new regime:

- Dividends received from subsidiaries located in a foreign country would qualify for the 95% exemption only if the country of establishment of the payer is included in the white list contained in the ministerial decree; and
- Italian parent companies would be taxed on 100% of the dividends received from a direct subsidiary established in a country not included in the white list.

A 27% withholding tax is imposed on dividends paid from Italian companies to nonresident companies without a permanent establishment in Italy (double tax treaties may provide for lower rates). Nonresidents may obtain a refund of dividend withholding tax equal to the amount of foreign tax paid on the dividends, but the maximum refund is 4/9 of the withholding tax paid. Under the 2008 Budget Law, dividends paid by Italian companies to entities established in an EU member state or in a country that is part of the European Economic Area (EEA) and included in the white list is subject to a 1.375% withholding tax. This new withholding tax rate applies to dividends paid in fiscal years beginning on or after 1 January 2008.

Companies from EU member states that receive dividends from Italian companies may be exempted from the dividend withholding tax or obtain a refund of the tax paid if they hold at least 15% of the shares of the payer for at least one year. The one-year holding period requirement must be satisfied as of the date of the distribution. The 15% threshold will be reduced to 10%, effective from 1 January 2009.

For nonresident companies with permanent establishments in Italy, the treatment of dividends is based on the principle of "PE attraction." Under this principle, dividends are deemed to flow through the Italian PE for tax purposes (unless a treaty provides otherwise), and no withholding tax applies.

## ***Withholding Taxes on Interest and Royalties***

Under Italian domestic law, a 12.5% withholding tax is imposed on loan interest paid to nonresidents. The rate is increased to 27% for payments to residents of black list (tax-haven) jurisdictions. Lower rates may apply under double tax treaties. Under the 2008 Budget Law, the 27% rate applies to companies resident in countries not included in the white list.

A 30% withholding tax applies to royalties and certain fees paid to nonresidents. In certain circumstances, the tax applies to 75% of the gross amount, resulting in an effective tax rate of 22.5%. Lower rates may apply under double tax treaties.

As a result of the implementation of EU Directive 2003/49/EC, withholding tax on interest payments and qualifying royalties paid between "associated companies" of different EU member states is abolished, effective from 1 January 2004. A company is an "associated company" of a second company if any of the following circumstances exist:

- The first company has a direct minimum holding of 25% of the voting rights of the second company;
- The second company has a direct minimum holding of 25% of voting rights of the first company; or
- A third company has a direct minimum holding of 25% of voting rights of both the first company and the second company.

Under the EU directive, the shareholding must be held for an uninterrupted period of at least one year. If the one-year requirement is not satisfied as of the date of payment of the interest or royalties, the withholding agent must withhold taxes on interest or royalties. However, if the requirement is subsequently satisfied, the recipient of the payment may request a refund from the tax authorities. To qualify for the withholding tax exemption, the following additional conditions must be satisfied:

- The recipient must be a company from another EU member state that is established as one of the legal forms listed in Annex B of the law;
- The income must be subject to tax in the recipient's jurisdiction, without any exemption; and
- The recipient must be the beneficial owner of the payment.

Domestic withholding taxes on interest and royalties may be reduced or eliminated by tax treaties.

### ***Foreign Tax Relief***

A foreign tax credit may be claimed for foreign-source income. The amount of the foreign tax credit cannot exceed that part of the corporate income tax, computed at the standard rate, that is attributable to the foreign-source income. Accordingly, the foreign tax credit may be claimed up to the amount that results from prorating the total tax due by the proportion of foreign-source income over total income. If income is received from more than one foreign country, the above limitation on the foreign tax credit is applied for each country (per-country limitation). Excess foreign tax credits may be carried forward or back for eight years.

For corporate groups that elect the worldwide tax consolidation (see Section C), an Italian parent company may consolidate profits and losses of its foreign subsidiaries joining the tax group and compute a single group tax liability. Such group tax liability may be offset by a direct foreign tax credit granted to the resident parent company with respect to taxes paid abroad by foreign subsidiaries that are members of the tax group.

## **C. Determination of Business Income**

### ***General***

To determine taxable income, profits disclosed in the financial statements are adjusted for exempt profits, nondeductible expenses, special deductions and losses brought forward. Exempt profits include interest on government bonds issued on or before 30 September 1986 and income subject to Italian withholding tax at source as a final tax. Interest on government bonds issued after 30 September 1986, however, is not exempt from tax.

The following general principles govern the deduction of expenses:

- Expenses are deductible if and to the extent to which they relate to activities or assets that produce revenue or other receipts that are included in income.
- Expenses are deductible in the fiscal year to which they relate (accrual basis rule). Exceptions are provided for specific items, such as compensation due to directors, which is deductible in the fiscal year in which it is paid.

Write-offs of the value of Italian and foreign shareholdings may not be deducted.

Companies may not deduct expenses incurred in transactions with enterprises resident in non-EU tax-haven countries. However, this limitation does not apply if it is established that either of the following conditions is satisfied:

- The foreign enterprise is effectively involved in an actual business activity in the country or territory in which it is located; or
- The relevant transactions had a real business purpose and actually took place.

The Ministry of Finance issued a decree dated 23 January 2002, which identifies the tax-haven countries. Under the 2008 Budget Law, the Ministry of Finance will issue a new decree providing a white list of countries that allow a satisfactory level of information exchange with the Italian tax authorities. Under a five-year grandfathering provision, countries that are not currently included in the applicable black list are considered to be on the white list.

### ***Thin Capitalization and Other Limitations on Interest Deductions***

Two sets of limitations are imposed on the deductibility of interest expenses accrued on the following:

- Loans obtained from or guaranteed by qualified shareholders or their related parties (thin capitalization); and
- Loans obtained to finance the acquisition of shares qualifying for the participation exemption (pro rata rule).

#### *Thin Capitalization.*

The thin-capitalization limitation applies to interest accrued on debts granted or guaranteed by a shareholder, or its related parties, that holds directly or indirectly a participation representing the majority of the voting rights or at least 25% of the share capital of the company. Companies in which the qualified shareholder holds a controlling interest are considered the shareholder's "related parties."

The thin-capitalization restriction applies when the ratio between the yearly average of related-party debt and the company's net equity exceeds 4: 1. Under the restriction, the deduction of interest on the debt exceeding the ratio is disallowed. The relevant debts include debts granted by direct or indirect shareholders or their controlled subsidiaries and third-party debts that are guaranteed by shareholders or their controlled subsidiaries.

To the extent that interest paid to related parties is disallowed because the debt-to-equity ratio exceeds 4: 1, such interest is treated as a dividend distributed by the company to the related-party lender. Banks and other financial companies (with the exception of insurance companies) are not subject to the thin-capitalization rules, except for companies that carry out exclusively or principally a holding activity. Accordingly, banks and financial companies may deduct without restriction interest accrued on debt granted or guaranteed by related parties. Companies, other than holding companies, that generate annual revenue of less than €7.5 million are not subject to the thin-capitalization rules.

#### *Pro Rata Rule*

The deductibility of interest may be restricted by the pro rata rule even if it is not restricted by the thin-capitalization rule. The pro rata rule applies to the portion of all interest payments (not only interest paid to related parties) that is not disallowed under the thin-capitalization rules.

Under the pro rata rule, the company's net equity is compared to its investment in subsidiaries (Italian and foreign) eligible for the participation exemption regime. The net equity is subject to certain adjustments designed to account for unpaid capital and uncovered operating losses.

If the book value of the investment in subsidiaries eligible for the participation exemption regime exceeds the adjusted net equity, the tax deduction for interest on related and unrelated debts is reduced by an amount calculated by applying the ratio of this excess amount to the amount by which total assets exceed adjusted net equity increased by trade payables. For the purpose of such limitation, the holding period for determining whether a participation qualifies for the pro rata rule continues to be 12 months.

Therefore, participations that have already been held for 12 months at the end of the fiscal year could reduce the company's ability to deduct interest expenses under the pro rata rule. The pro rata rule does not apply to subsidiaries that elect tax consolidation or consortium relief (see *Groups of Companies* below).

Under the draft 2008 Budget Bill, both the pro rata rule and the thin-capitalization rule would be repealed. Consequently, the deductibility of interest expenses would depend only on an Earnings Before Income Taxes, Depreciation and Amortization (EBITDA) test resembling the one that is effective in Germany from the 2008 fiscal year. Under this test, the excess of interest expenses over interest income would be nondeductible to the extent that this excess amount is greater than 30% of the accounting gross profit. Any nondeductible amounts arising in the 2008, 2009 and 2010 fiscal years would be carried forward for 10 years. The carryforward period would be five years for nondeductible amounts arising in the 2011 fiscal year and future fiscal years.

### ***Foreign-Exchange Losses***

Gains and losses resulting from the mark-to-market of foreign currency-denominated debts, credits and securities are not relevant. An exception is provided for those hedged against exchange risk if the hedging is correspondingly marked-to-market at the exchange rate at the end of the fiscal year.

### ***Non-operating Companies***

Italian resident companies and permanent establishments of nonresident companies are deemed to be "non-operating companies" if the total of their average non- extraordinary revenues (proceeds from the ordinary activities of a company as shown on its financial statements) and increases in inventory are less than the sum of the average of the following during the preceding three years:

- 2% of the book value of the company's financial assets;
- 6% of the book value of the company's real estate assets; and
- 15% of the book value of the company's other long term assets.

If the company qualifies as a non-operating company, its taxable income cannot be lower than the sum of the following items:

- 1.5% of the book value of the company's financial assets for the year;
- 4.75% of the book value of the company's real estate assets for the year; and
- 12% of the book value of the company's other long-term assets for the year.

Non-operating companies that are in a value-added tax (VAT) credit position may no longer take the following actions:

- Claim such VAT for a refund;
- Use the VAT to offset other tax payments due;
- Surrender the VAT to other group companies; or
- Carry forward the VAT.

Tax losses incurred by non-operating companies may not be carried forward.

Companies can be exempted from the above mentioned regime, for both income tax and VAT purposes, if they prove to the tax authorities that they were not able to reach the minimum income requirements because of extraordinary circumstances (an advance ruling must be obtained for such a determination). Certain companies are specifically excluded from the non-operating companies' regime (for example, listed groups). The 2008 Budget Law provides additional exclusions, such as companies with 50 or more shareholders and companies with an amount of business income greater than the total asset value

### ***Inventories***

Inventory is normally valued at the lower of cost or market value for both fiscal and accounting purposes. However, companies may select other methods of inventory valuation specifically provided in the law, such as first-in, first-out (FIFO), last-in, first-out (LIFO) or average cost.

### ***Provisions***

Italian tax law provides a limited number of provisions.

#### ***Bad and Doubtful Debts***

A general provision of 0.5% of total trade receivables at the year-end may be made each year until the total doubtful debt provision reaches 5%. Bad debts actually incurred are deductible to the extent they are not covered by the accumulated reserve and only if they have become irrecoverable or if there are bankruptcy proceedings.

Banks may deduct on a straight-line basis over nine years the write-down of receivables that exceeds the 0.4% limitation described in the preceding paragraph.

#### ***Redundancy and Retirement Payments***

Provisions for redundancy and retirement payments are deductible in amounts stated by civil law and relevant collective agreements.

### ***Depreciation and Amortization Allowances***

Depreciation at rates not exceeding those prescribed by the Ministry of Finance is calculated on the purchase price or cost of manufacture. Incidental costs, such as customs duties and transport and installation expenses, are included in the depreciable base. Depreciation is computed on the straight-line method. Rates for plant and machinery vary between 3% and 15%. The established rates may be increased if assets are more intensely used than they are normally. For the first three years of an asset's life, anticipated depreciation of up to two times the ordinary rate per year may be claimed.

Under the 2008 Budget Law, accelerated depreciation (increased depreciation as a result of more intense use of the asset and anticipated depreciation claimed during the first three years of an asset's life) is no longer allowed. Consequently, only a deduction equal to half the ordinary depreciation in the year of acquisition is allowed.

In general, buildings may be depreciated using a 3% annual rate. Land may not be depreciated. If a building has not been purchased separately from the underlying land, for tax purposes the gross value must be divided between the non-depreciable land component and the depreciable building component.

The land component may not be less than 20% of the gross value (increased to 30% for industrial buildings). As a result, the effective depreciation rate for buildings is 2.4% (2.1% for industrial buildings).

Purchased goodwill may be amortized over a period of 18 years. Know-how, copyrights, and patents may be amortized over two fiscal years. The amortization period for trademarks is 18 years.

Research expenses and advertising expenses may be either entirely deducted in the year incurred or written off in equal installments in that year and in the four subsequent years, at the company's option.

Amortization allowances of other rights may be claimed with reference to the utilization period provided by the agreement.

### ***Relief for Losses***

For IRES purposes only, losses may be carried forward and deducted from income of the five subsequent tax periods. Stricter rules apply to loss carry-forwards if ownership of the company is transferred and if the company changes its activities. Effective from 2006, certain limitations on tax loss carry- forwards that applied to transfers of companies to third parties are extended to intra-group transfers.

Losses incurred in the first three years of an activity may be carried forward for an unlimited number of tax periods. Effective from 2006, the three-year time limit is no longer computed from the date of the beginning of the company's activities, but from the company's date of incorporation. In addition, to qualify for an unlimited loss carry-forward, such losses must derive from a new activity; that is, companies within the same group may not have previously carried out the activity.

The company resulting from or surviving after a merger may carry forward unrelieved losses of the merged companies against its own profits for the unexpired portion of the loss carryforward periods.

In general, tax losses carried forward may not exceed the lower of the net equity at the close of the last fiscal year or the net equity shown on the statement of net worth prepared for the merger of each company involved in the merger. This limitation is applied on a company-by-company basis.

Contributions to capital made in the 24 months preceding the date of the net worth statement are disregarded. Special rules further limit the amount of the losses that can be carried forward. Additional measures combat abuses resulting from the use of losses with respect to mergers, demergers and the transparency regime (see *Consortium Relief below*)

### ***Groups of Companies***

Groups of companies may benefit from tax consolidation and consortium relief. These regimes allow the off- setting of profit and losses of members of a group of companies.

#### *Tax Consolidation.*

Italian tax consolidation rules provide two separate consolidation systems, depending on the residence of the companies involved. A domestic consolidation regime is available for Italian resident companies only. A worldwide consolidation regime, with slightly different conditions, is available for multinationals.

To qualify for consolidation, more than 50% of the voting rights of each subsidiary must be owned, directly or indirectly, by the common Italian parent company.

For a domestic consolidation, the election is binding for three fiscal years. However, if the holding company loses control over a subsidiary, such subsidiary must be immediately excluded from the consolidation. The tax consolidation includes 100% of the subsidiaries' profits and losses, even if the subsidiary has other shareholders. The domestic consolidation may be limited to certain entities, leaving one or more otherwise eligible entities out- side the group filing election. Tax losses realized before the election for tax consolidation can be used only by the company that incurred such losses.

Although, in general, intracorporate dividends are 95% exempt (that is, 5% of the dividends are taxable), dividends within the consolidated group are 100% exempt. Under the 2008 Budget Law, this measure is repealed and all intracorporate dividends, including dividends within a consolidated group are 95% exempt.

Under a domestic consolidation, transfers of assets (other than goods produced or traded by the company, shares, bonds, and other similar securities) between group members may be carried out as tax-neutral transactions if both the seller and the buyer elect the domestic consolidation regime. Under the 2008 Budget Law, the transfer of assets within consolidated companies becomes a taxable transaction, unless qualifying for tax-free treatment under other specific rules provided by the Italian tax laws.

#### *Consortium Relief*

Italian parent corporations can elect consortium relief if they hold more than 10% but less than 50% of the voting rights in their Italian subsidiaries. Under this election, the subsidiaries are treated as look-through entities for Italian tax purposes and their profits and losses flow through to the parent company in proportion to the stake owned. These profits or losses can offset the shareholders' losses or profits in the fiscal year in which the transparent company's fiscal year ends. Tax losses realized by the shareholders before the exercise of the election for the consortium relief cannot be used to offset profits of transparent companies.

Dividends distributed by an eligible transparent company are not taken into account for tax purposes in the hands of the recipient shareholders. As a result, Italian corporate shareholders of a transparent company are not subject to corporate income tax on 5% of the dividends received.

The election does not change the tax treatment of dividends distributed out of reserves containing profits accrued before the exercise of the election. Another benefit from consortium relief is that an eligible transparent company does not pay corporate income tax.

The consortium relief election is binding for three fiscal years and requires the consent of all the shareholders.

The consortium relief election may be beneficial for joint ventures that are not eligible for tax consolidation because the control test is not met. In addition, the election is also available for non-resident companies that are not subject to Italian withholding tax on dividend payments (that is, EU corporate shareholders qualifying under the EU Parent-Subsidiary Directive). If both EU corporate shareholders qualifying under the EU Parent-Subsidiary Directive and Italian corporate shareholders hold an Italian subsidiary, the EU corporate shareholders would want to elect consortium relief to allow the Italian corporate shareholders to benefit from tax transparency.

#### *Group Value-Added Tax*

For groups of companies linked by more than a 50% direct shareholding, net value-added tax (VAT; see Section D) refundable to one group company with respect to its own transactions may be offset against VAT payable by another, and only the balance is required to be paid by, or refunded to, the group.

## **D. Other Significant Taxes**

The table below summarizes other significant taxes.

<i>Nature of Tax</i>	<i>Rate</i>
Value-added tax, on goods, services and imports	
Standard rate	20%
Other rates	4%/10%
Municipal real property tax (Id),	

imposed on property's cadastral value	0.4% to 0.7%
Transfer tax on disposals of shares	0.14%
Social security contributions (2007 rates); includes employee's liability, pension contributions (IVS) and other minor contributions Industry; payable on gross remuneration by employers with more than 50 employees	
Workers	41.57%
Office staff	39.35%
Executives	36.45%
Additional contribution payable to the Social Security Institute for Industrial Executives (PREVINDAI); based on gross remuneration capped at €150,000	8%
Additional contribution payable for industrial executives to other social insurance fund (FASI)	
Employer	quarterly €360/ annual €1,440
Employee	quarterly € 183/ annual €732
Trade; payable on gross remuneration by employers with more than 200 employees	
Workers	39.37%
Office staff	39.37%
Executives	36.03%
(For workers with remuneration greater than €40,083, the above rates are increased by 1%. For workers not making social security contributions before 1 January 1996, the pension contributions [IVS] payable by employers and employees is calculated on gross salary capped at €87,187.)	

***Nature of Tax***

***Rate***

Contribution for industrial injuries or professional diseases; payable by employers; rate depends on the professional risk covered (income caps apply to executives)	0.5% to 1.3%
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**E. Miscellaneous Matters**

***Foreign-Exchange Controls***

The underlying principle of the foreign- exchange control system is that transactions with nonresidents are permitted unless expressly prohibited. However, payments by residents to foreign intermediaries must be channeled through authorized banks or professional intermediaries. In addition, transfers of money and securities exceeding € 10,000 must be declared to the Italian Exchange Office. Inbound and outbound investments are virtually unrestricted.

***Transfer Pricing***

Italy imposes transfer-pricing rules on transactions between related resident and nonresident companies. Under these rules, intra-group transactions must be carried out at arm's length. The Italian

transfer-pricing rules do not apply to domestic transactions. As a result, adjustments of the prices in these transactions are based on other anti-abuse provisions.

### ***Controlled Foreign Companies***

Italian law provides for the following two categories of controlled foreign companies (CFCs):

- Controlled companies (under Article 1 67 of the Income Tax Code); and
- Associated companies (under Article 1 68 of the Income Tax Code).

#### *Controlled Companies.*

If an Italian individual or company controls directly or indirectly a company established in a black list (tax haven) jurisdiction, the individual or company's share of the income of the CFC is attributed to the individual or company, regardless of distribution. The income of the CFC must be assessed using the Italian corporate income tax rules and is taxed at the average rate of the Italian shareholder, but no lower than 27%.

#### *Associated Companies.*

If an Italian individual or company owns directly or indirectly 20% of a company established in a black list (tax haven) jurisdiction (10% if the company is listed), the individual or company's share of the income of the CFC is attributed to the individual or company, regardless of distribution. The income of the CFC is assessed as the higher of the following amounts:

- Earnings before tax on the basis of the accounts; or
- A minimum income determined by applying certain ratios (1% for financial assets, 4% for real estate and 1 5% for other assets) to the assets of the CFC.

### **Anti-avoidance Legislation**

Under Italian anti-avoidance rules (Article 37-bis of Presidential Decree No. 600/1973), in principle, the tax authorities may consider a transaction that involves single or connected acts to be a tax-avoidance transaction if it meets all of the following requirements at the same time:

- The transaction involves one or more of the following operations:
  - Contributions to companies or transfers or use of going concerns;
  - Assignments of credits;
  - Assignments of excess tax credits;
  - Payments of interest and royalties that are exempt from withholding tax (see Section B) to EU companies that are directly or indirectly controlled by non-EU residents;
  - Transactions provided for in EU Directive No. 90/434/CEE (the Merger Directive);
  - Transactions, including appraisals, regarding participations, securities, certificates, currencies, precious metals, swaps, options, hedging instruments and other specified items; and Transfers of assets carried out as tax-neutral transactions between companies electing the domestic group taxation regime (see Section C).
- The transaction was entered into without a valid business purpose.
- The transaction was entered into in order to get around the law.
- The transaction was entered into in order to achieve an undue income tax savings or tax refunds.

The tax authorities may disregard a tax-avoidance transaction for tax purposes. The anti-avoidance rules may be applied only to income tax and to estate and gift tax under an express reference.

### *Debt-to-Equity Rules*

For information regarding thin-capitalization rules and other restrictions on the deductibility of interest, see Section C.

### *Mergers and Acquisitions*

The 2008 Budget Law provides a significant change to the rules for the fiscal treatment of values resulting from merger and acquisitions transactions. Under the law, companies undertaking mergers, demergers, and asset contributions in exchange for shares may step up the tax basis of the assets by paying an 18% step-up tax. The step-up election applies to mergers and transactions, effective from the 2008 fiscal year. However, for operations finalized by 31 December 2007, the realignment of the tax and accounting basis of assets recorded in the 2007 financial statements and tax return is allowed if the 18% tax is paid.

### *F. Treaty Withholding Tax Rates*

	<i>Dividends (1)</i>	<i>Interest</i>	<i>Royalties</i>	
Albania	10	0/5 (d)(e)(z)	5	
Algeria	15	0/15 (d)(e)(z)	5/15	(o)
Argentina	15	0/20 (d)(e)(z)	10/18	(h)
Australia	15	0/10 (d)	10	
Austria	15	0/10 (d)(e)(z)	0/10	(i)
Bangladesh	10/15 (a)	0/10/15 (d)(e)(y)	10	
Belgium	15	0/15 (w)	5	
Brazil	15	0/15 (d)	15/22.5	(k)
Bulgaria	10	0	5	
Canada	15	0/15 (d)(e)(z)	0/10	(l)
China	10	0/10 (d)(tt)	7/10	(aa)
Côte d'Ivoire	15/18 (uu)	0/15 (d)	10	
Cyprus	15 (ww)	10	0	
Czechoslovakia (t)	15	0	0/5	(h)
Denmark	0/15 (a)	0/10 (ee)(mm)	0/5	(nn)
Ecuador	15	0/10 (d)(e)(z)	5	
Egypt	20/27 (cc)	0/25 (d)(e)(z)	15	
Estonia	5/15 (a)	0/10 (d)(vv)	5/10 (kk)	
Ethiopia	10	0/10 (oo)	20	
Finland	10/15 (a)	0/15 (d)(e)(z)	0/5 (o)	
France	5/15 (a)(gg)	0/10 (d)(e)(z)(ee)	0/5 (o)	
Georgia	5/10 (a)	0	0	
Germany	10/15 (a)	0/10/12.5 (d)(e)(z)(ee)(ff)	0/5 (l)	
Ghana	5/15 (a)	10	10	
Greece	15	0/10 (d)(e)(z)	0/5 (m)	
Hungary	10	0	0	
India	15/25 (a)	0/15 (d)(e)	20	
Indonesia	10/15 (a)	0/10 (d)(e)(z)	10/15 (x)	
Ireland	15	10	0	
Israel	10/15 (a)	10	0/10 (o)	
Japan	10/15 (a)	10	10	

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Kazakhstan	5/15 (a)	0/10 (d)(e)(z)	0/10 (hh)
Korea	10/15 (a)	0/10 (d)(e)(vv)	10
Kuwait	5/27 (a)	0	10
Lithuania	5/15 (a)	10 (d)(e)(z)	5/10 (kk)
Luxembourg	15	0/1 0 (d)(e)(z)	10
Macedonia	5/15 (a)	10 (d)(e)(z)	0
Malaysia	10 (xx)	0/15 (d)	15
Malta	15	0/10 (d)(e)(z)	0/10 (m)
Mauritius	5/15 (a)	0/12.5/27 (dd)	15
Mexico	15	0/1 5 (d)(e)(z)	0/1 5 (l)
Morocco	10/15 (a)	0/10 (d)(e)(z)	5/10 (o)
Mozambique	15	0/1 0 (11)	10
Netherlands	5/10/15 (c)	0/10 (d)(e)(z)	5
New Zealand	15	0/10 (d)(e)(z)	10
Norway	15	0/15 (d)(e)(z)	5
Oman	5/10 (pp)	0/5 (oo)	10
Pakistan	15/25 (a)	0/27 (d)(e)(z)	22.5 (k)
Philippines	15	0/10/15 (d)(e)(z)	22.5 (k)
Poland	10	0/10 (d)(e)(z)	10
Portugal	15	0/15 (d)(e)(z)	12
Romania	10	0/10 (d)(e)(z)	10
Russian Federation	5/10 (g)	10	0
Senegal	15	15 (11)	15
Singapore	10	0/12.5 (d)(z)	15/20 (n)
South Africa	5/1 5 (a)	0/1 0 (d)(e)(z)	6
Spain	15	0/12 (d)(e)(z)	4/8 (o)
Sri Lanka	15	0/10 (d)(e)(z)	10/15 (q)
Sweden	10/15 (a)	0/15 (d)(e)(z)	5
Switzerland	15	12.5 (rr)	5
Syria	5/10 (a)	0/10 (qq)	18
Tanzania	10	15	15
Thailand	15/20 (a)	0/10 (d)(e)(j)	5/15 (h)
Trinidad and Tobago	1 0/20 (a)	10	0/5 (bb)
Tunisia	15	0/12 (d)(e)	5/12/16 (r)
Turkey	15	15	10
Uganda	15	0/15 (b)(z)	10
Ukraine	5/15 (a)	0/10 (11)	7
USSR(u)	15	0/12.5/27(u)	—
United Arab Emirates	5/15 (a)	0	10
United Kingdom	5/15 (a)(gg)	0/10 (e)(ee)	8
United States	5/10/15 (c)	0/15 (d)	5/7/8/10 (s)
Uzbekistan	10	0/5 (11)	5
Venezuela	10	0/10 (b)(z)	7/10 (p)
Vietnam	5/10/15 (f)	10 (d)(e)(z)	7.5/10 (jj)
Yugoslavia (v)	10	10	10
Zambia	5/15 (a)	0/10 (d)	10
Non-treaty countries	27 (ss)	12.5/27 (ss)	22.5

- (1) Dividends paid by Italian companies to EU parent companies are exempt from withholding tax if the recipient company holds a participation of at least 15% (10% from 2009) in the distributing company for an uninterrupted period of at least one year.
- (a) The lower rate applies to corporate shareholders satisfying the following qualifying tests: Bangladesh, Estonia, India, Kazakhstan and Lithuania: at least 10% of the capital; Denmark: at least 25% of the capital for 12 months before the date the dividend is distributed; Finland: more than 50% of the capital; France: more than 10% of the capital for 12 months; Georgia, Germany, Indonesia, Israel, Korea, Macedonia, Mauritius, Morocco, Pakistan, Syria, Trinidad and Tobago, United Arab Emirates and Zambia: at least 25% of the capital; Ghana: at least 10% of the capital; Japan: at least 25% of the shares with voting rights for six months; Kuwait: at least 75% of the capital; South Africa: at least 25% of the capital for 12 months ending on the date the dividend is declared; Sweden: at least 51% of the capital; Thailand: at least 25% of the shares with voting rights; Ukraine: at least 20% of the capital; and United Kingdom: at least 10% of the shares with voting rights for 12 months.
- (b) The 0% rate applies to interest paid to or by a government.
- (c) The 5% rate applies to corporations that beneficially own more than 50% of the voting rights of the shares for 12 months ending on the date the dividend is declared. The 10% rate requires 10% ownership. The 15% rate applies in all other cases.
- (d) Interest paid to a “government” or central bank is exempt. The term “government” refers to the central government and any other local authority entirely owned by the state that receives interest on behalf of the central authority.
- (e) Interest paid by a contracting state is exempt. Under the Philippines treaty, the loan must involve the issuance of bonds or financial instruments similar to bonds.
- (f) The 5% rate applies to dividends paid to corporations that beneficially own at least 70% of the capital of the payer. The 10% rate applies to dividends paid to corporations that beneficially own at least 25% but less than 70% of the capital of the payer. The 15% rate applies to other dividends.
- (g) The 5% rate applies if the recipient of the dividend is a corporation that beneficially owns more than 10% of the capital of the payer and if the value of the participation of the recipient is at least US\$100,000 or an equivalent amount in another currency. The 10% rate applies to other dividends.
- (h) The lower rate is for the use of or right to use literary, artistic and scientific copyrights.
- (i) The higher rate applies if the recipient has an investment exceeding 50% of the capital of the payer.
- (j) The 10% rate applies only if the payer is engaged in an industrial activity and the interest is paid to a financial institution (including an insurance company). The exemption also applies to bonds issued by a contracting state.
- (k) Because the tax rates provided by these treaties (Brazil, 25%; and Pakistan, 30%) are higher than the rate under domestic law, the domestic rate of 22.5% applies. For Brazil, the 22.5% rate applies to trademark royalties only.
- (l) The lower rate applies to royalties for literature, plays, and musical or artistic works. Under the Germany treaty, royalties for films and recordings for television qualify for the lower rate. Under the Canada treaty, such royalties do not qualify for the lower rate. Under the Mexico treaty, royalties for films and recordings for television and radio do not qualify for the lower rate.
- (m) The lower rate applies to royalties paid for literary, artistic or scientific works and for films and recordings for radio or television.
- (n) The lower rate applies to patents, trademarks, trade names or other intellectual property.
- (o) The lower rate applies to royalties from the use of copyrights on literary, artistic or scientific works (excluding cinema and television films).
- (p) The lower rate applies to royalties paid for the use of, or the right to use, copyrights for literary, artistic or scientific works, including cinematographic films and recordings for radio and television broadcasts.
- (q) The lower rate applies to royalties paid for literary and artistic works, including films and recordings for radio and television.
- (r) In the case of royalties for the use of trademarks, films and industrial, commercial or scientific equipment, the withholding is 16%; for the use of copy- rights for artistic, literary and scientific works, the rate is 5%. In all other cases, the rate is 120%.
- (s) In the case of royalties for the use of literary, artistic and scientific works, the rate is 5%; for the use of tangible property, the rate is 7%; for the use of films and recordings for radio or television, the rate is 8%. In all other cases, the rate is 10%.
- (t) The Czechoslovakia treaty applies to the Czech and Slovak Republics.
- (u) In general, the USSR treaty is honored by the Commonwealth of Independent States (CIS), except for Kazakhstan, but CIS members have different positions on the treaty. Italy and Kazakhstan have entered into a tax treaty (see rates in table).
- (v) The treaty with the former Yugoslavia applies to Croatia, Slovenia and the Federal Republic of Yugoslavia. Italy has entered into a new tax treaty with Macedonia.
- (w) An exemption applies to the following:
- Interest on loans that are not in the form of bearer securities if the interest is paid to the following: the other contracting state; its political or administrative subdivisions; or its local authorities; and
  - Interest paid to credit institutions of the other contracting state if the interest is paid on loans that are not in the form of bearer securities and if the loans are permitted under an agreement between the governments of the contracting states.
- (x) The 10% rate applies to royalties and commissions paid for the use of or right to use the following: industrial, commercial or scientific equipment; or information concerning industrial, business or scientific know-how. The 15% rate applies to other royalties.
- (y) The 10% rate applies to interest paid by banks and other financial entities ( that is, insurance companies). The 15% rate applies to other interest.
- (z) Interest paid on loans made in accordance with an agreement between the governments of the contracting states is exempt. Under the Mexico treaty, the loan must have a term of at least three years.

(aa) Payments for the use of industrial, commercial and scientific equipment are taxed on the basis of 70% of the gross payments. Consequently, the effective rate for such payments is 7%.

(bb) The lower rate applies to royalties for literature, musical and artistic works. (cc) The 27% rate is the rate under Italian domestic law for dividends paid to nonresidents.

(dd) These are the rates under Italian domestic law. Under the treaty, the rate is 0% if the interest is paid to a Mauritian public body or bank resident in Mauritius.

(ee) Exemption is provided for interest paid in connection with the following:

- Credit sales of industrial, commercial or scientific equipment; and
- Credit sales of goods delivered from one enterprise to another enterprise.

(ff) The 12.5% rate applies to payments on profit-sharing loans and to silent partners. The 10% rate applies in other circumstances.

(gg) A refund may be available for the underlying tax credit with respect to business profits attached to the dividends.

(hh) If a resident of a contracting state receives payments for the use of, or the right to use, industrial, commercial or scientific equipment from sources in the other contracting state, the resident may elect to be taxed in the contracting state in which the royalties arise as if the property or right for which the royalties are paid is effectively connected with a permanent establishment or fixed base in that contracting state. If such election is made, no withholding tax is imposed on the payments.

(ii) The treaty exempts the following types of interest:

- Interest on bank credits and loans; and
- Interest on current accounts and deposits with banks or other credit institutions.

The 12.5% and 27% rates are the withholding tax rates under Italian domestic law.

(ii) The lower rate applies to fees paid for technical assistance services. The higher rate applies to royalties paid for the use of the intangibles.

(kk) The 5% rate applies to royalties paid for the use of industrial, commercial or scientific equipment.

(ll) The treaty provides the following exemptions:

- Interest paid by the government or its local authorities;
- Interest paid to the government of the other contracting state or its local authorities or other entities and organizations (including credit institutions) wholly owned by the other contracting state or its local authorities; and
- Interest paid to other entities and organizations (including credit institutions) if the interest is paid on loans permitted under an agreement between the governments of the contracting states.

(mm) The treaty provides the following exemptions:

- Interest paid by the state of source, its political or administrative subdivisions or its local authorities; and
- Interest paid on loans granted, guaranteed or secured by the government of the other contracting state, by its central bank or by other entities and organizations (including credit institutions) wholly owned by the other contracting state or under its control.

(nn) The lower rate applies to royalties paid for the use of, or the right to use, copyrights for literary, artistic or scientific works, excluding cinematographic films and other audio and visual recordings.

(oo) The treaty provides the following exemptions:

- Interest paid by the government or a local authority thereof;
- Interest paid to the government, a local authority thereof or an agency or instrumentality (including a financial institution) wholly owned by the other contracting state or a local authority thereof; and
- Interest paid to any other agency or instrumentality (including a financial institution) with respect to loans made under agreement entered into between the governments of the contracting states.

(pp) The 5% rate applies to companies (other than partnerships) that hold directly at least 1 5% of the capital of the payer of the dividends. The 10% rate applies to other dividends.

(qq) The treaty provides the following exemptions:

- Interest paid to a contracting state, a local authority thereof, or a corporation having a public status, including the central bank of that state;
- Interest paid by a contracting state or local authority thereof, or any corporation having a public status;
- Interest paid to a resident of a contracting state with respect to debt obligations guaranteed or insured by that contracting state or by another person acting on behalf of the contracting state;
- Interest paid with respect to sales on credit of industrial, commercial or scientific equipment or of goods or services between enterprises; and Interest paid on bank loans.

(rr) Effective from 1 July 2005 a 0% rate may apply under the agreement between Switzerland and the EU. The rates shown in the table are the withholding tax rates under the Italy-Switzerland double tax treaty. Subject to fulfillment of the respective requirements, the taxpayers may apply either the Switzerland-EU agreement or the Italy-Switzerland double tax treaty.

(ss) See Section A.

(tt) The exemption applies to interest paid to a resident of the other contracting state with respect to debt claims indirectly financed by the government of that other contracting state, a local authority, the central bank thereof or a financial institution wholly owned by the government of the other contracting state.

(uu) The 18% rate applies to dividends paid by a company established in Côte d'Ivoire that is exempt from income tax or not subject to the normal income tax rate

(vv) The lower rate applies to interest related to loans that are guaranteed by the government or a local authority. Under the Korea treaty, the guarantee must be evidenced by an agreement contained in an exchange of letters between the competent authorities of the contracting states.

(ww) The 15% rate applies to dividends paid by a company established in Italy to a Cyprus resident beneficiary. Dividends paid by a company established in Cyprus to an Italian resident beneficiary are exempt from withholding tax in Cyprus.

(xx) The 10% rate applies to dividends paid by an Italian company to a Malaysian resident. Dividends paid by a Malaysian company to an effective beneficiary resident in Italy are exempt from tax in Malaysia if the beneficiary is subject to tax on the dividends in Italy.