MAISTO E ASSOCIATI

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Highlights

- Review of the black lists announced
- Amendments to the recently introduced "Patent Box" regime
- Extension of the interest withholding tax exemption for qualifying foreign lenders
- Supreme Court judgments on the application of gift tax to trusts
- Foreign tax credit: clarifications provided by the Italian tax authorities
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1. Review of the black lists announced

The Ministry of Finance has announced the issuance of two new decrees replacing the currently existing "black lists" applicable for the purposes of CFC rules and anti-tax haven deduction rules, in application of the amendments introduced by the 2015 Finance Act (see Tax Alert 1/2015).

Pursuant to such changes:

- the CFC black list has been revised to exclude all countries that have an adequate exchange of information and a tax rate not lower than 50% of the tax rate applicable in Italy. The countries that are no longer black-listed for the purposes of the CFC rules are Singapore, Malaysia and the Philippines;
- the anti-tax haven deduction black list has been revised to exclude all countries that have an adequate exchange of information with Italy. The countries that are no longer black-listed for such purposes include the Channel Islands, the Netherlands Antilles, Bermuda, British Virgin Islands, the United Arab Emirates, Mauritius, Malaysia, Singapore and the Philippines.

For certain countries (including Switzerland) the black-listing has been extended. Indeed, in the previous drafting of the black list, for such countries only certain tax regimes were black-listed, whereas in the revised black list the entire country is considered black-listed due to the absence of an adequate exchange of information.

The decrees will delegate the Tax Agency to issue another list of tax regimes that still fall under the CFC black list (even if in countries with an ordinary tax rate higher than 50% of the Italian rate) because their effective tax rate goes below 50%.

2. Amendments to the recently introduced "Patent Box" regime

As outlined in our previous Tax Alert 10/2014, as from 1 January 2015 a new “patent box” regime has been introduced in Italy.

With Decree Law No. 3/15, converted into law No. 33/2015 (“**Investment Compact Decree**”) a number of amendments to the new regime have been introduced, aimed at further encouraging the repatriation of IP currently held abroad and discouraging the transfer abroad of IP currently held in Italy. The changes also seem in line with the “modified nexus approach” jointly proposed by Germany and United Kingdom within the OECD Forum on Harmful Tax Practices (FHTP) and later endorsed by the OECD on 6 February 2015 in the Report “Action 5. Agreement on Modified Nexus approach for IP Regimes”.

As a result of the changes introduced by the Investment Compact Decree:

- the scope of the “patent box” regime has been broadened to “designs” and "models”, as well as to all “trademarks” (including marketing trademarks);
- the access to the regime has been extended to qualifying taxpayers that do not internally conduct the R&D activity but outsource it (provided that not all of the R&D activity is outsourced to related parties);
- the portion of income qualifying for the tax benefit has been redefined by partially computing also the R&D activities outsourced to related parties and the IP acquisition costs (up to 30% of the total qualifying R&D costs);
- it is clarified that the option for the application of the “patent box” regime is renewable;
- with respect to the determination of the qualifying income arising from intercompany licensing, it has been provided that the application for an Advance Pricing Agreement (APA) is optional and not mandatory.

The implementing decrees of the “patent box” regime are still awaited.

3. Extension of the interest withholding tax exemption for qualifying foreign lenders

The Investment Compact Decree also further extended the withholding tax exemption recently introduced for interest on medium-long term loans granted to Italian enterprises. In particular, the class of lenders that are eligible for domestic exemption, which previously applied to unleveraged EU/EEA collective investment undertakings, has been broadened to include all institutional investors, even if not qualified as taxpayers in their State of establishment, that are established in a white-listed State and are subject to regulatory supervision therein.

The exemption also applies to EU established banks, EU insurance companies and certain EU non-banking State owned entities that grant loans in the exercise of their institutional functions.

4. Supreme Court judgments on the application of gift tax to trusts

The Supreme Court recently issued four judgments on the application of gift tax to the creation of trusts.

In all four judgments, the Court upheld the approach of the tax authorities that is to levy gift tax upon the addition of assets to the trust fund, rather than upon distribution to the beneficiaries (such approach was rejected so far by the large majority of the first and second degree courts).

In judgments No. 3735/15 and No. 3886/15, the Court clarified that gift tax applies also upon the creation of a self-declared trust, even if the creation does not entail any transfer of assets. The position of the Court is grounded on the fact that, for trusts, the taxable event is the creation of the lien over the assets, rather than the transfer of the assets.
In judgment No. 3886/15, the Court also upheld the view of the tax authorities that, to the extent that the beneficiaries include the settlor, the applicable gift tax rate is the highest 8% rate, since the 4% and 6% rates apply only if the donee or the beneficiary of the trust is a close relative to the settlor.

In judgments No. 3737/15 and No. 5322/15, the Court ruled that the creation of a purpose trust, to fund the development and maintenance of a local airport for a 5-year period, is subject to gift tax at the 8% rate. The trust deed provided that, at the end of the above mentioned 5-year period, the assets still belonging to the trust fund would be appointed to a local entity, which would be selected by the settlors: with respect to such specific cases, the decision of the Court implies that such a distribution, which entails a new destination for the assets directed by the settlor, qualifies as a separate taxable event.

5. Foreign tax credit: clarifications provided by the Italian tax authorities

On 5 March 2015, the Italian tax authorities issued Circular No. 9/E, providing extensive guidelines on the application of domestic foreign tax credit provisions set forth by Article 165 Income Tax Act ("**ITA**").

Among other things, the tax authorities took the view that, in order not to adversely treat distributions from non-Italian partnerships that are tax transparent in their foreign State of establishment, distributions to resident partners are subject to Italian income tax on the amount net of the foreign taxes due by the partners and that no foreign tax credit is available to the partners. This interpretation is meant to take into account that foreign partnerships are fiscally opaque under Italian law and, therefore, to treat distributions from foreign partnerships in the same way as dividends from foreign corporate vehicles. The new interpretation is certainly beneficial in relation to non-substantial participations, for which the domestic tax legislation does not provide for any foreign tax credit, since distributions are taxed at a flat rate of 26%.

On the other hand, the new interpretation seems to depart from previous positions of the Italian tax authorities, which, in relation to substantial participations in non-resident partnerships that are fiscally transparent in their foreign State of establishment, had recognized the entitlement of partners to a foreign tax credit (not just the deduction of the foreign tax from the Italian taxable base).

Moreover, the Circular clarified that foreign taxes which do not qualify for the Italian foreign tax credit system under art. 165 ITA may still be deducted for corporate income tax purposes. The clarification mainly addresses the case of business income subjected to tax in a foreign State, but that does not qualify as foreign-source income for Italian tax purposes (e.g. because Italy does not recognize a foreign permanent establishment) and therefore does not qualify for any foreign tax credit under domestic rules.

Furthermore, the tax authorities took the view that the foreign tax credit is granted for foreign-source income realized through Italian permanent establishments of non-resident companies (or individuals). The conclusion is grounded, according to the tax authorities, on the permanent establishment non-discrimination provision contained in Art. 24(3) of treaties patterned along the lines of the OECD Model Convention.

6. Extension of "reverse brain drain" incentive

The "reverse brain drain" incentive, consisting of a 80% (women) and 70% (men) exemption regime from income tax for qualifying EU nationals, originally laid down by law No. 238 of 30 December 2010, has been extended until 31 December 2017. The regime applies to EU nationals born after 1st January 1969 who, after continuously residing for at least 24 months in Italy, have been working or studying outside their home country and Italy for at least 2 years, and subsequently regain residency for Italian tax purposes.

The exemption is retrospectively revoked and ordinary income taxes plus penalties and interests are applied if the EU national subsequently ceases to be Italian tax resident before 5 years from its transfer of residence to Italy.

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