Making an offer

International Tax



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Guido Pignanelli and Malachy McLernon explain the Italian 'voluntary disclosure' system

Key Points

What is the issue?

Italy enforced a new provision enabling the government to regulate many ‘irregular’ tax structures

What does it mean for me?

It might be an interesting opportunity for any individuals or corporations that have been running a business in Italy over past eight to 10 years. The provisions enable penalties to be reduced and avoid criminal charges

What can I take away?

The expiry date of this opportunity is 30 September 2015. Interested parties have to be aware of it now.

Law n.186/2014 enforced a ‘voluntary disclosure’ provision on 1 January this year, entitling taxpayers to disclose several kinds of violations of the Italian tax laws. To better illustrate the opportunity of this law, a brief review of the Italian tax system will be helpful.

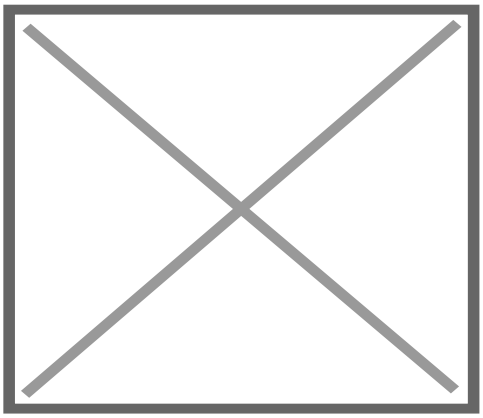
Personal tax

Italian residents are subject to a personal income tax (IRPEF) computed on a worldwide basis, in accordance to a cash-received principle.

In addition, individuals carrying on a business or a profession are liable to the payment of a regional tax (IRAP). Non-resident individuals are subject to taxes only on their Italian source income.

Progressive rates for IRPEF are set out in ***Box 1***.

Box 1 – Italian resident personal income tax rates



Corporate tax

Corporate income tax (IRES) is payable by all resident companies on their worldwide income and is charged at 27.5%; also, companies are subject to the regional tax (IRAP) at 3.9%.

Non-resident companies or entities are subject to Italian corporate tax on business activity only if they run their business through a permanent establishment based in Italy. Withholding taxes are applicable on the flow of income of Italian source (dividends, interests and royalties). Italian legislation has implemented European Directive 90/435/EEC (Parent/Subsidiary Directive), under which no withholding tax is levied on dividends paid to a parent company in another EU member state if both the parent and the subsidiary qualify as companies, and the parent has been holding at least 10% of the capital of the subsidiary continuously for at least one year.

The EU Interest and Royalties Directive has also been incorporated into domestic law. Outbound interest and royalties are exempt from any Italian tax as long as the recipient is an associated company of the paying company and is resident in another EU member state or if such a company’s permanent establishment is in another member state. A one-year holding period is required.

Branch profit tax

An Italian branch of a foreign company is fully liable to IRES and IRAP. Italy enforced a standard definition of permanent establishment, namely a fixed place of business through which a foreign company carries on its business within Italy. Its legal existence is not separate from the company that controls it. Corporate formalities required to set up and run a branch are less of a burden than those required for a

subsidiary. A branch is not required to hold shareholders' meetings or to appoint statutory auditors. It is allowed to repatriate profits at any time. On the other hand, since the branch and the foreign company of which it is part remain one legal entity, the latter is not immune from branch liabilities. Indeed, the foreign company may be held liable for debts or damages arising out of the transactions of the branch, such as product liability claims.

Fiscal monitoring of assets held abroad

Resident individuals, partnerships and non-commercial entities must comply with the obligations of fiscal monitoring by disclosing to the Italian revenue agency all the assets held anywhere in the world, regardless of their value. Real estate, deposits at foreign banks, and ownership (shares or interest) held in non-resident companies must be disclosed in the RW section on the Italian income tax return. Until fiscal year 2013, the penalties for misrepresentations on this section were high; they were reduced after an infringement procedure issued by the EU Commission against Italy.

The section must be completed by both the formal holder of the assets and the beneficial owner of the assets themselves. For instance, should a trust (both resident in Italy or outside Italy) be only formally the holder of the assets held abroad, the RW section must be completed by the individuals 'behind' the trust.

Who is an Italian resident for tax purposes?

Individuals are considered tax resident in Italy if one of these conditions is met for more than six months in any calendar year:

- registered at the official register of population; or
- their principal place of business and interest is in Italy; or
- their permanent residence address is in Italy.

Companies are considered resident in Italy when, for most of the fiscal year, at least one of these conditions is met:

- the registered office of the company is in Italy;
- the managing office of the company is in Italy; and
- the main activity of the business is carried out in Italy.

The foreign companies controlling Italian companies are deemed to be resident in Italy if:

- they are controlled by an Italian resident subject; or
- the majority of the directors are Italian residents.

It is also worth noting that a trust is qualified as Italian-resident for fiscal purposes when it has been incorporated in a tax haven (like Jersey) where at least one of the settlors and at least one of the beneficiaries are resident in Italy.

The Italy-UK tax treaty: concept of residence

The Italy-UK treaty article 4 is in line with the OECD's international standard template. According to the treaty, when an individual might be qualified as resident of both countries, then the following 'tie breaker rules' have to be referred to:

- if the taxpayer has a permanent home available to them in both contracting states, the centre of vital interests must be investigated;
- if both the available permanent home and centre of vital interests features cannot be determined, they shall be deemed to be a resident of the state in which they have a habitual abode; and
- if they have a habitual abode in both contracting states, or in neither of them, they shall be deemed to be a resident of the contracting state of which they are a national.

Should these not be helpful for assigning the residence of the taxpayer, the question is settled by the local authorities.

The new Italian 'voluntary disclosure' provision

The Law n.186/2014, in force from 1 January this year, approved the voluntary disclosure provisions that foresee a declaration taking place when the taxpayer spontaneously provides some information to the Italian tax authorities.

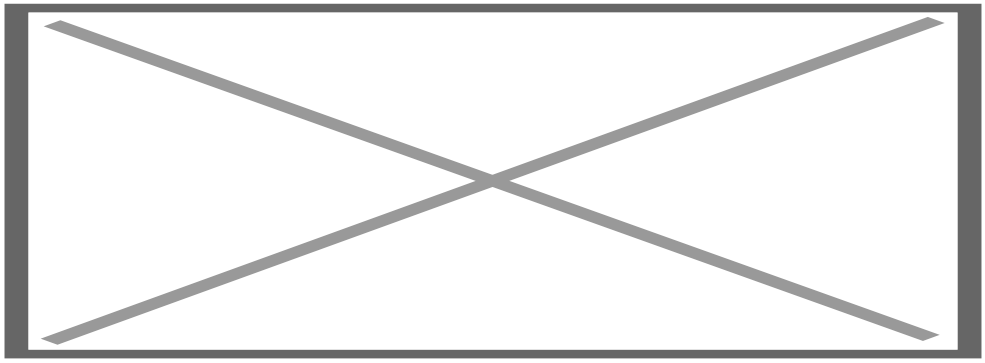
The application cannot be submitted for situations already undergoing either tax inspection or assessment. The above mentioned information must be provided no later than 30 September 2015 and it must cover any fiscal years for which the statute of limitation has not expired when the application was filed.

Table 1 summarises the periods anticipated by Italian law relating to the statute of limitation. The periods still subject to tax assessment are doubled when, alternatively:

- the assets are held in ‘blacklisted’ countries; and
- the violation is subject to the laws foreseen by the Italian penal code.

Two different procedures are foreseen by the recent voluntary disclosure law.

Table 1 – Voluntary disclosure periods



Voluntary disclosure of undeclared foreign assets

Resident individuals, partnerships and non-commercial entities are allowed to regulate, from a tax perspective, all assets and other investments for which the laws governing the monitoring of assets held abroad were not respected. The voluntary disclosure might be useful to a non-Italian taxpayer, such as a UK multinational executive who has been transferred to Italy and likely to be qualified as resident there over some years. As a consequence, they should have declared all their assets on a worldwide basis (for example, on a UK bank account). So, should an ‘expatriate’ realise that they were not compliant with the Italian laws governing the monitoring of assets held abroad, they can now use the disclosure procedure.

To benefit from the disclosure, the taxpayer must provide the tax authorities with any useful information in order to:

- identify all the assets held abroad;
- identify the income used to constitute such investments abroad; and
- identify any possible income arising from their disposal or use.

After receiving the application, the Italian tax authorities will calculate the liabilities for both the undeclared taxable basis and violations of monitoring laws, along with applicable interest and penalties. The administrative penalties, usually equal to unpaid taxes, will be calculated at the lowest rate, reduced by 25%.

National voluntary disclosure

As well as international voluntary disclosure, a national voluntary disclosure is now available, applicable for most tax law violations (declaration and/or payment of taxes) connected with:

- Income tax;
    - corporate income tax (IRES),
    - substitute/withholding tax,
    - regional tax on productive activities (IRAP); and
- Value added tax (VAT).

The national voluntary disclosure applies to taxes on financial and non-financial assets, regardless of whether they are in Italy or abroad. Such an opportunity might be interesting to non-resident entities that have not properly declared taxable assets held in Italy. For a UK company, this might be interesting in the case of a developing Italian business, for which the existence of an Italian permanent establishment was not declared – the voluntary disclosure might be the right way to solve a risky ongoing situation.

Effects of voluntary disclosure

The taxpayer who applies for voluntary disclosure (and those who have broken the rules) is also immune from most of the criminal tax penalties imposed by Legislative Decree no.74/2000, as well as from the money laundering penalties recently imposed by the penal code. Any person filling a voluntary disclosure form is granted immunity from prosecution for certain fiscal offences such as:

- fraudulent misrepresentation using invoices, non-existent transactions or other mechanisms (articles 2 and 3);
- misrepresentation (article 4);
- failure to declare (article 5);

- non-payment of certified withholding tax (article 10-bis); and
- non-payment of VAT (article 10-ter).

The voluntary disclosure procedure is properly finalised by the payment of taxes, otherwise the application (either international or national) will be invalid.

New agreements concluded with previous ‘blacklist countries’

At the beginning of 2015, Italy signed additional agreements, based on the OECD Model Tax Information Exchange Agreement (TIEA), which authorises the exchange of information on request with Switzerland, Liechtenstein and Monaco.

These agreements significantly affect the voluntary disclosure procedure. Having been signed no later than 2 March 2015, such countries are no longer considered blacklisted for voluntary disclosure purposes. On the other hand, these countries can no longer be regarded as a safe harbour by a taxpayer who, in the past, has hidden assets there from the Italian revenue agency.

A statement of practice, which is soon to be issued by the director of the Italian revenue agency, will clarify the rules on how to submit the application, paying the amounts due and other technical and operational features. It is important to mention that a preliminary analysis of all documentation is recommended to determine in advance the portion of income that Italian tax authorities will qualify as taxable and to calculate the tax due. For international voluntary disclosure, greater caution is needed for recent increases of undeclared assets. To minimise the tax burden, the taxpayer must prove that such an increase cannot be entirely qualified as undeclared income.

Economic overview of Italy

Italy has a longstanding trade relationship with the UK. It’s the world’s ninth largest economy with a gross domestic product (GDP) of USD$2014.6 billion in 2012 and is Europe’s second largest manufacturer behind Germany.

Italian companies are globalising. Most are small and medium-sized enterprises (SMEs) which require professional services to grow internationally.

Benefits for British businesses exporting to Italy include:

- EU market, so no tariffs;
- similar regulatory framework to the UK;
- easy access from the UK with low-cost flights from several regional airports;
- gateway to Mediterranean markets; and
- one of the world’s highest rates of household wealth.

Strengths of the Italian market include:

- modern infrastructure;
- high level of internationalisation and entrepreneurship;
- strong manufacturing and innovation capability in several areas;
- hosts many trade exhibitions with global appeal; and
- one of the world’s top five tourist destinations.

Trade between the UK and Italy

Bilateral trade in goods was valued at £23.5 billion in 2013. In 2013 Italy was the ninth largest market for UK goods exports, totalling £8,385 million, 6% up on 2012.

The main exports of goods by value from the UK to Italy in 2013 were:

- road vehicles;
- machinery and mechanical appliances, boilers;
- pharmaceutical products;
- electrical machinery;
- audio and TV equipment; and
- mineral fuels, oils and distillation products.

British companies ranked fourth by turnover and employees in the list of foreign investors in Italy as of January 2012.