Bloomberg Tax

International Tax News®

NUMBER 0 MAY 10, 2019

INSIGHT: Italy Introduces Brexit Law

BY GUIDO ARIE PETRAROLI AND FRANCESCO CARDONE

The Italian Hard Brexit Decree (the Decree) introduced urgent measures in order to ensure security, financial stability and market integrity in case of withdrawal of the U.K. from the EU without the ratification of the withdrawal agreement.

The Decree was published in the Italian Official Gazette on March 25, 2019 and entered into force on March 26, 2019.

It shall be converted into law by the Italian Parliament within 60 days of its publication otherwise it will be retroactively ineffective. In the conversion phase the Italian Parliament could amend the current version of the Decree.

On April 10, 2019, the European Council, upon request of the U.K., decided to extend the two-year period referred to in Article 50, paragraph 3, of the Treaty on European Union to allow for the ratification of the withdrawal agreement.

As specified in the European Council's conclusions, such an extension should last only as long as necessary and, in any event, no longer than October 31, 2019. In a no-deal scenario, the U.K. will become a third country as from November 1, 2019 since the Treaty on European Union and the Treaty on the Functioning of the European Union will cease to apply to the U.K. from such date.

Despite the extension until October 31 decided by the European Council, the Decree still applies because, if the withdrawal agreement is not ratified, the Decree will apply in a no-deal scenario.

Guido Arie Petraroli is Managing Partner and Francesco Cardone is a Director at LED Tax-and, Italy

18-month Transitional Period for Tax Purposes

Article 13 of the Decree introduces a general transitional period for tax purposes, which will last for 18 months from the date of the withdrawal of the U.K. from the EU in absence of a withdrawal agreement.

According to the Decree, during the transitional period the following Italian tax provisions will continue to apply to the U.K.:

- Italian tax provisions applicable only to EU member states;
- Italian tax provisions deriving from the implementation of EU tax directives;
- Italian tax provisions deriving from the implementation of EU directives and regulations related to value-added tax (VAT) and excise duty, as far as compatible.

The Decree specifies that one or more decrees to be issued by the Italian Ministry of Economy and Finance will introduce procedures and terms for the implementation of the above-mentioned transitional tax provision.

Italian Tax Provisions Applicable only to EU Member States

Based on the Decree, during the transitional period the Italian tax provisions applicable by virtue of being a member of the EU will also apply to the U.K. Examples of this type of Italian tax provisions, which generally in-

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troduce more favorable regimes for EU countries, are summarized below.

Article 47-bis of the Income Tax Code in identifying foreign low-tax regimes excludes the ones available in EU or in European Economic Area (EEA) countries. Dividends and capital gains derived from companies benefiting from a low-tax regime are in principle fully taxable for individual income tax (IIT) and corporate income tax (CIT) purposes.

Article 117 of the Income Tax Code related to the domestic tax consolidation regime also includes the horizontal tax consolidation which applies if resident sister companies are commonly controlled by a parent company that is resident in an EU or EEA country.

Article 26, paragraph 5-bis, Presidential Decree No. 600/1973 provides for a withholding tax exemption on interest payments under medium/long-term loans granted to Italian enterprises by banks established in the EU.

Article 27, paragraph 3, Presidential Decree No. 600/1973 provides for a reduced withholding tax on dividends paid to pension funds established in an EU or EEA country.

Article 27, paragraph 3-ter, Presidential Decree No. 600/1973 provides for a reduced withholding tax on dividends paid to entities subject to CIT in an EU or EEA country.

Article 1, paragraph 1, Legislative Decree No. 239/1996 provides for a withholding tax exemption on interest payments on bonds: (i) issued by companies whose shares are traded on regulated markets or multilateral trading systems of an EU or EEA country; or (ii) traded on regulated markets or multilateral trading systems of an EU or EEA country.

Article 10-ter Law No. 77/1983 provides for a final 26 percent withholding tax on proceeds derived by resident individuals from Undertakings for Collective Investment in Transferable Securities (UCITS) established in an EU or EEA country instead of their full taxation for IIT purposes (whose marginal rate is 43 percent).

Article 17 Presidential Decree No. 601/1973 provides for a substitute tax in relation to medium- and long-term financing (i.e. maturity exceeding 18 months) granted by banks established in an EU country, insurance companies established and authorized in an EU country and investment funds established in an EU or EEA country.

Article 19, paragraph 15, Law Decree No. 201/2011 related to IVIE (tax on foreign immovable properties held by resident individuals) specifies that in case of immovable properties situated in an EU or EEA country the taxable base is its value relevant for foreign tax purposes instead of the acquisition cost or its fair market value.

Article 16, paragraph 5, Ministerial Decree 21 February 2013 provides for an exemption from the Tobin tax for pension funds subject to supervision under the Directive 2003/41 (now 2016/2341) and compulsory social security institutions established in an EU or EEA country.

Article 1, paragraphs 119 and 141-bis, Law No. 296/2006 introduced the optional SIIQ regime for (i) Italian real estate companies whose shares are traded on EU or EEA regulated markets and (ii) Italian permanent establishments of companies resident in an EU or EEA country.

Italian Tax Provisions Deriving from EU Tax Directives

According to the Decree, during the transitional period the Italian tax provisions deriving from the implementation of EU tax directives will apply also to the U.K. Examples of these type of Italian tax provisions are summarized below.

The Parent-Subsidiary Directive (2011/96) during the transitional period will keep eliminating juridical double taxation (granting a withholding tax exemption in the source state) and economic double taxation (requiring the residence state to exempt the dividend received or to grant a tax credit) if all the conditions are met. While after the transitional period, the domestic 26 percent withholding tax should apply to dividends paid to shareholders resident in the U.K. which could be reduced to 5 percent/15 percent under the Italy–U.K. tax treaty, if applicable.

The Interest and Royalty Directive (2003/49) will apply during the transitional period granting a withholding tax exemption in the source state on intra-group interest and royalty payments, if all the conditions are met. While after the transitional period, the domestic 26 percent withholding tax should apply to interest paid to beneficiaries resident in the U.K. which could be reduced to 10 percent under the Italy–U.K. tax treaty, if applicable. Domestic 30 percent withholding tax should apply to royalties which could be reduced to 8 percent under the treaty.

The Merger Directive (2009/133) during the transitional period will continue to ensure tax neutrality, under certain conditions, on cross-border reorganizations such as mergers, divisions, partial divisions, transfers of assets and exchanges of shares concerning companies of different EU member states.

The Anti-Tax Avoidance Directive (2016/1164) was implemented in Italy introducing specific favorable provisions applicable only to EU member states. For example, in line with Article 4, paragraph 4(b), of the Anti-Tax Avoidance Directive, the Italian interest limitation rule does not apply to interest expenses incurred on loans used to fund a long-term public infrastructure project where the project operator and the assets related to the project are in a EU member state. Moreover, in line with Article 5, paragraph 2, of the Anti-Tax Avoidance Directive, the Italian exit tax regime provides that the taxpayer has the right to defer the payment of such tax, by way of installments over a five-year period, only in relation to transfer to an EU or EEA country.

The Directive on Administrative Cooperation (2011/16) related to exchange of information and the Recovery Assistance Directive (2010/24) will continue to apply in the transitional period. After the transitional period, the U.K. will exchange information and recover taxes cross-border according to the OECD Convention on Mutual Administrative Assistance in Tax Matters and its bilateral tax treaties.

The Arbitration Convention (90/436) related to the elimination of double taxation in connection with the adjustment of profits of associated enterprises should continue to apply since it is a multilateral convention.

VAT and Excise Duty

Based on the Decree, during the transitional period the Italian tax provisions deriving from the implementation of EU directives and regulations related to VAT and excise duty will continue to apply, as far as compatible.

As regards the Excise Duty Directive (2008/118), on February 22, 2019, the Italian Customs Agency issued guidelines on trade flows of excise goods (e.g. alcoholic beverages, wine and beer) to and from the U.K. in a no-deal scenario.

In relation to the VAT Directive (2006/112) and the Union Customs Code (952/2013), on February 26, 2019, the Italian Customs Agency issued guidelines specifying that, in a no-deal scenario, flows of goods to and from the U.K. will qualify as export and import for VAT and Custom purposes.

In light of the Decree published on March 25, 2019, in a no-deal scenario, the Italian Customs Agency guidelines described above should apply after the transitional period.

Summary

Italy has introduced tax measures aimed at ensuring stability in case of a hard Brexit scenario.

In particular, the Decree introduced an 18-month transitional period for tax purposes where all the Italian tax provisions applicable only to EU member states or deriving from the implementation of EU tax directives will continue to apply to the U.K.

In addition, the Italian Customs Agency issued guidelines on excise duty, VAT and Customs duty in case of a no-deal scenario.

Lastly, on April 10, 2019, the Italian tax authorities established the information service point ''Info Brexit,'' in order to reply to questions submitted by resident and nonresident taxpayers in relation to the withdrawal of the U.K. from the EU.

Planning Points

Although the tax consequences of Brexit are still unclear, they might lead to massive changes for certain taxpayers, requiring significant time to adapt to the new scenario.

Therefore, every taxpayer with relationships with the U.K. should start evaluating the potential consequences.

As highlighted in this article, from an Italian tax viewpoint, the analysis of the post-Brexit scenarios should take into account:

- Italian tax provisions applicable only to EU member states;
- Italian tax provisions deriving from the implementation of EU tax directives;
- Italian tax provisions deriving from the implementation of EU directives and regulations related to VAT and excise duty.

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