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Italian Revenue Office clarifications on CFC rules

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After the Italian Revenue Office issued new guidance on CFC regulations, Piergiorgio Valente from Valente Associati GEB Partners reviews the changes.

Introduction

On August 4 2016, the Italian Revenue Office issued Circular No. 35/E (the circular) on rules and regulations for controlled foreign corporations (CFCs).

The circular provides clarifications on identification criteria involving countries with privileged tax regimes as well as on the treatment of profits deriving from such countries.

It falls within the framework of the most recent regulatory innovations on the subject-matter which had some repercussions on both the taxation regime of income produced by foreign controlled companies and taxation of profits deriving from so-called "tax haven" countries.

The new rules mentioned above are contained in Legislative Decree No. 147 of September 14 2015 (*Decreto Internazionalizzazione*), providing measures for entrepreneurial development and internationalisation. The latter's objective is to help Italy become more attractive and competitive for Italian or foreign enterprises planning to invest in Italy.

There is indeed a growing awareness with regard to the impact the tax variable may have on operators' economic choices and of the role the tax system may play in its activities to support entrepreneurial internationalisation through the reduction of cross-border obligations, and the creation of a regulatory framework that is reliable and transparent.

Low-tax regimes and taxation of profits

The circular provides elucidations on the criteria to identify privileged tax regimes, starting from January 1 2016. These are exclusively based on a nominal taxation level of less than 50% vis-à-vis the applicable taxation level in Italy and are no longer based on the formal criterion of a country's inclusion in the black-list.

A clear description of the applicable criteria related to the 2015 tax period is also provided. Through an interpretative reading, the exclusion of EU or EEA member states that guarantee adequate information exchange from privileged tax regimes (a notion of provided by the Italian 2016 Stability Law) was extended to also include the 2015 tax period.

As far as the nominal tax level is concerned, the circular specifically states that from the Italian side, in line with the traditional black-list criteria and pursuant to Ministerial Decree dated November 21 2001, tax-relevance is ascribed to the corporate income tax (IReS) rate that was applicable during the tax period to which the control requirement refers, without taking any surtax into account. Italian Regional Tax on Productive Activities (IRAP), the ordinary tax rate of which (3.9%) is being considered, is also tax-relevant.

The circular further provides clarification on the notion of deriving profits, and clear-cut details on the treatment of dividends and capital gains, which are the expression of prior profits.

In order to establish whether the dividends are actually derived or sourced from a tax haven, the criterion that was applicable at the time of their receipt is taken into account. It is precisely at this point in time that taxation occurs, and is established, at the taxpayer's level.

For dividends received and for capital gains realised up until the entry into force of Ministerial Decree of March 30 2015, and for blacklist inclusion or exclusion, ex Ministerial Decree dated November 21 2001, is still a valid aspect. While for the ones realised after such date, special attention should be paid to both inclusion in the black list and – in any case – to the stated criterion of a "taxation level of 50% lower than the one applied in Italy".

For distributed dividends and capital gains realised as of 2016, the "nominal taxation level (...) 50% lower than the one applicable in Italy" applies, regardless of the criterion that was in force at the time in which the profit of the participated company was generated.

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