Investing in Italian Real Estate Assets through Collective Investment Vehicles: An Overview of Tax Implications for Foreign Investors

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The author provides a comprehensive analysis of the Italian tax regime for real estate investment funds and SICAFs, focusing on both the vehicles and the investors.

1. Introduction

Real estate investments in Italy by foreign institutional investors can be carried out via two different types of regulated collective investment vehicles,[1] namely real estate investment funds (*fondi comuni di investimento immobiliare*, REIFs) and real estate closed-ended investment companies (*SICAF immobiliari*, R-SICAFs), both of which offer an attractive tax regime.

REIFs and R-SICAFs (collectively referred to as "R-UCIs") are both undertakings for collective investments (*organismi di investimento collettivo del risparmio*, OICR) (UCIs) that primarily invest in real estate assets and rights, the difference being that a REIF is set up in a contractual common fund form (i.e. it is not a legal entity, but rather a pool of investments jointly held by multiple unit holders), while an R-SICAF is set up in corporate form. They both qualify as alternative investment funds (AIFs) under the provisions implementing the Alternative Investment Fund Managers Directive (AIFMD)[2] in Italy.

The regulatory and tax framework for the above-mentioned investment vehicles has been enacted or reshaped more or less recently. Indeed, the regulations on SICAFs (including R-SICAFs) were passed in 2014 and 2015, in implementation of the AIFMD. Italy has transposed the AIFMD through Legislative Decree 44 of 4 March 2014 (AIFMD Decree), which includes significant changes to the tax and regulatory framework concerning UCIs and introduced SICAFs as a new form of UCI set up in corporate form. The REIF regime, which was first introduced in 1994, has been amended several times over the years. The current rules, enacted in 2010 and 2011 after a series of legislative changes, were fine tuned in 2014 and 2015.

This article will outline the attractive tax regime applicable to REIFs and R-SICAFs, as well as the tax treatment of the proceeds derived by foreign investors in R-UCIs.

2. Legal and Regulatory Overview

2.1. General overview

The primary law applicable to UCIs is Legislative Decree 58 of 24 February 1998 (the Finance Code). The Finance Code is complemented by the AIFMD Decree and by several statutes and regulations issued by the Bank of Italy, the Ministry for Economic Affairs and the Italian regulatory authority for financial markets (*Commissione Nazionale per le Società e la Borsa*, more commonly known as "CONSOB"), namely:

- the CONSOB regulation implementing the Finance Code adopted by Resolution 11971 of 14 May 1999 (the CONSOB Regulation);
- the Bank of Italy Regulation on UCIs of 19 January 2015 (the Bank of Italy Regulation); and
- Ministry of Economic Affairs Decree 30 of 5 March 2015 enacting certain provisions of the Finance Code (the Ministry of Economic Affairs Decree).

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1. As an alternative, the investments can also be carried out through ordinary real estate companies (*società immobiliari*, RE-Cos) or listed real estate investment companies (*società di investimento immobiliare quotate*, SIIQ). A RE-Co is a special purpose vehicle, formed as a limited liability company (*società a responsabilità limitata*, S.r.l.) or as a joint-stock company (*società per azioni*, S.p.A.), carrying out the purchase, management, leasing, building and/or sale of Italian real estate assets. A SIIQ is a joint-stock company the shares of which are listed on a regulated market of an EU Member State or a European Economic Area (EEA) Member State and the main business of which is the leasing of real estate assets. A SIIQ must comply with certain specific requirements set out by the law, and benefits from a favourable tax regime (in this regard, a new law passed in Sept. 2015 made the tax regime of SIIQs more attractive for Italian and foreign institutional investors, aligning it with the tax regime applicable to R-UCIs). SIIQs are comparable to real estate investment trusts, even though by provision of law they do not qualify as UCIs.
2. Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) 1060/2009 and (EU) 1095/2010, OJ L 174 (2011), EU Law IBFD.

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2.2. UCIs: Definition and requirements

According to the Finance Code,[3] a UCI is:

> an undertaking set up to provide collective management services, the assets of which are collected from a plurality of investors by means of the issue and offer of units or shares, managed on a pooled basis in the interest of the investors and independently from them, and invested in financial instruments, credits, including those advanced to persons different from consumers, using their own assets, shareholdings or other movable or non-movable assets, on the basis of a pre-defined investment policy.[4]

In light of this definition, from a regulatory perspective UCIs must satisfy the following requirements (the UCI requirements):

- raising capital from a plurality of investors;[5]
- adoption of a pre-defined investment policy;
- pooled investment of the capital for the benefit of the investors; and
- autonomous and independent management.

Satisfaction of these UCI requirements (in particular, the "plurality of investors" requirement and the "autonomous and independent management" requirement) is also a key element for purposes of tax analysis, as the beneficial tax regime for UCIs in general (and R-UCIs in particular) applies only to regulatory compliant undertakings (*see* below).

The definition of "Italian UCIs" (*OICR italiani*)[6] includes common funds (*fondi comuni d'investimento*),[7] open-ended investment companies (*società di investimento a capitale variabile*, SICAV)[8] and closed-ended investment companies (*società di investimento a capitale fisso*, SICAF).[9] SICAVs, however, are not an available option for real estate investments.[10]

2.3. REIFs versus R-SICAFs

As mentioned, an Italian REIF is not a legal entity (with separate legal personality), but rather a pool of real estate investments jointly held by multiple unitholders, managed on their behalf and in their interest by an external asset management company. Accordingly, REIFs are externally managed AIFs.

On the other hand, a SICAF (including an R-SICAF) is a closed-ended UCI established in the form of a joint-stock company with fixed capital. It is, therefore, an incorporated investment fund and, as such, it may be more familiar and appealing to foreign investors than a REIF. A SICAF may be managed by the relevant board of directors or by an external asset management company. Therefore, depending on the relevant management model adopted, SICAFs can be internally managed AIFs[11] or externally managed AIFs.

The asset management company (in the case of REIFs and externally managed SICAFs) can be an Italian asset management company (*società di gestione del risparmio*, SGR) or, subject to a number of conditions and formalities, an EU AIF manager (EU AIFM) or a non-EU AIF manager (non-EU AIFM).[12]

2.4. Investment restrictions

According to the Ministry of Economic Affairs Decree,[13] R-UCIs must be invested (in an exclusive or prevalent manner) in real estate assets, *in rem* real estate rights (including those arising from financial leasing contracts implying a transfer of ownership and from public concession agreements), equity interests in real estate companies and shares/units of Italian or foreign real estate UCIs (these being the

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3. Art. 1(1)(k) Finance Code, as amended by the AIFMD Decree and, subsequently, by Decree 91 of 24 June 2014 and by Decree 18 of 14 Feb. 2016. The definition in art. 1(1)(k) is inspired by the wording of art. 4(1)(a) AIFMD, whereby AIFs are "collective investment undertakings, including investment compartments thereof, which: (i) raise capital from a number of investors with a view to investing it in accordance with a defined investment policy for the benefit of those investors; and (ii) do not require authorization pursuant to Article 5 of Directive 2009/65/EC [the UCITS Directive]".
4. Author's translation.
5. The requirement that there be a plurality of investors may be met even where there is only one investor, provided that it represents itself a plurality of investors.
6. Art. 1(1)(l) Finance Code. Italian UCIs include "mutual funds, SICAVs and SICAFs" (author's translation).
7. Art. 1(1)(j) Finance Code. A mutual fund is "a UCI established in the form of an autonomous pool of assets, subdivided in units, established and managed by a fund manager" (author's translation).
8. Art. 1(1)(i) Finance Code. A SICAV is "an open-ended UCI established in the form of joint-stock company with variable capital, registered office and general management in Italy, having as exclusive purpose that of the collective investment of the capital raised by means of the offer of shares" (author's translation).
9. Art. 1(1)(i-bis) Finance Code. A SICAF is "a closed-ended UCI established in the form of joint-stock company with fixed capital, registered office and general management in Italy, having as its exclusive purpose that of the collective investment of the capital raised by means of the offer of shares and other participating financial instruments" (author's translation).
10. Indeed, R-UCIs may be set up only as closed-ended undertakings (art. 12(1) Ministry of Economic Affairs Decree). Moreover, SICAVs are not allowed to invest in real estate properties or rights. This is also consistent with the definition of Italian real estate AIFs in art. 1(1)(q) Ministry of Economic Affairs Decree, which includes only funds and SICAFs that invest in real estate assets and rights.
11. An internally managed R-SICAF also qualifies as an AIFM.
12. According to the Finance Code, EU AIFMs and non-EU AIFMs are allowed to set up and manage Italian AIFs (including, therefore, REIFs and R-SICAFs), provided that, amongst other issues, they are authorized in their home state to manage AIFs with comparable features.
13. Art. 12(2), first sentence, Ministry of Economic Affairs Decree.

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"typical investments"). At least two thirds of the assets of an R-UCI must be invested in assets and rights falling within the notion of typical investments. The ratio is reduced to 51% if the undertaking also invests no less than 20% of its assets in financial instruments representing securitization transactions where the underlying assets are represented by real estate property, real estate rights or mortgage-secured receivables.[14] An R-UCI must satisfy the above investment thresholds (two thirds or 51%, as the case may be) within 24 months from the start of its operations.[15]

3. Tax Framework

3.1. General overview

The tax rules applicable to Italian REIFs are mainly contained in Decree 351 of 25 September 2001 (Decree 351/01), in article 32 of Decree 78 of 31 May 2010 (Decree 78/2010) as amended by Decree 70 of 13 May 2011 (Decree 70/2011) and in the implementing Regulations enacted by the tax authorities on 16 December 2011 (the Regulations).[16] In particular:

- articles 6 and 7 of Decree 351/01, article 32 of Decree 78/2010 and the Regulations establish the income tax regime for REIFs and their investors; and
- article 8 and 9 of Decree 351/01 lay out certain VAT and transfer tax rules.

According to the AIFMD Decree, these provisions also apply to R-SICAFs.[17]

These rules have been commented by the Italian tax authorities in Circular 11/E of 9 March 2011 (Circular 11/E/2011),[18] Circular 2/E of 15 February 2012 (Circular 2/E/2012),[19] Ruling 54/E of 18 July 2013 (Ruling 54/E/2013)[20] and Circular 21/E of 10 July 2014 (Circular 21/E/2014).[21]

3.2. Corporation tax and local tax regime

3.2.1. Introduction

Under Decree 917 of 22 December 1986[22] (Decree 917/86), Italian resident UCIs (including REIFs and R-SICAFs) qualify as "non-commercial entities" (*enti non commerciali*) and are amongst the taxpayers that fall under the scope of corporation tax[23] (IRES, generally levied at the rate of 27.5%).[24] A UCI is deemed to be tax resident in Italy when it is established therein.[25] In this respect, the tax authorities clarified in Circular 21/E/2014 that a UCI is deemed to be tax resident in Italy when established on the basis of Italian rules, regardless of whether the management company is resident in Italy or elsewhere.

As better explained below, regulatory compliant REIFs and R-SICAFs are exempted from IRES.[26] , [27] REIFs are exempted from local tax (IRAP, generally levied at the rate of 3.9%, with possible regional variances), as well. On the other hand, SICAFs (including R-SICAFs) are subject to the same IRAP regime applicable to SICAVs;[28] accordingly, they are liable to IRAP, but the taxable base is limited to the difference between the subscription fees (*commissioni di sottoscrizione*) and the fees due to placement agents (*commissioni passive dovute a soggetti collocatori*).

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14. Art. 12(2), second sentence, Ministry of Economic Affairs Decree.
15. Art. 12(2), third sentence, Ministry of Economic Affairs Decree. In some circumstances, the term is extended from 24 months to 48 months.
16. The Regulations are available at http://www.agenziaentrate.gov.it/wps/wcm/connect/bda347004971e1f08119d55f3f895a05/180987+decreto+fondi+immobiliari+16dic+pulito.pdf?MOD=AJPERES&CACHEID=bda347004971e1f08119d55f3f895a05.
17. Art. 9(1) AIFMD Decree states that the tax provisions applicable to REIFs, contained e.g. in art. 6 et seq. Decree 351/01 and in art. 32, will be applicable to SICAFs that carry out real estate investments in compliance with the thresholds set out in the civil law provisions.
18. Circular 11/E/2011 is available at http://www.agenziaentrate.gov.it/wps/wcm/connect/2582ef00460ffd9195dcdf51d5b740d9/Circ.11e+del+09.03.11.pdf?MOD=AJPERES&CACHEID=2582ef00460ffd9195dcdf51d5b740d9.
19. Circular 2/E/2012 is available at http://www.agenziaentrate.gov.it/wps/wcm/connect/2d5438804a2d800e8855ada7ae7bbfda/circolare+2e.pdf?MOD=AJPERES&CACHEID=2d5438804a2d800e8855ada7ae7bbfda.
20. Ruling 54/E/2013 is available at http://www.agenziaentrate.gov.it/wps/file/nsilib/nsi/documentazione/provvedimenti+circolari+e+risoluzioni/risoluzioni/archivio+risoluzioni/risoluzioni+2013/luglio+2013+risoluzioni/risoluzione+54+18072013+regime+di+tassazione/RIS+54e+del+18+07+2013.pdf.
21. Circular 21/E/2014 is available at http://www.agenziaentrate.gov.it/wps/file/nsilib/nsi/documentazione/provvedimenti+circolari+e+risoluzioni/circolari/archivio+circolari/circolari+2014/luglio+2014/circolare+n.+21e+del+10+luglio+2014/Circ+21_E+del+10+lug+2014.pdf.
22. The Italian Income Tax Code.
23. Art. 73(1)(c) Decree 917/86. In this respect, it is worth noting that a SICAF is a corporation that, by being a UCI from a regulatory standpoint, is included amongst the "non-commercial entities" for IRES purposes.
24. The IRES rate will drop to 24% from 2017. Indeed, art. 1(61) Law 208 of 28 Dec. 2015 reduced the IRES rate, stating that the 24% rate would apply from the tax period following the one in progress at 31 Dec. 2016.
25. Art. 73(3) Decree 917/86.
26. Despite being exempted from IRES, R-UCIs may still be liable to a 26% final (i.e. unrecoverable) withholding tax that is deducted at source from certain categories of financial income, such as interest on certain bonds and interest on financial instruments that qualify as atypical securities (i.e. they do not satisfy the requirements for being treated as equities or as bonds).
27. While R-UCIs may be exempted from IRES under art. 6 Decree351/01, all other UCIs may be exempted as well by provision of art. 73(5-quinquies) Decree 917/86. The exemption under art. 73(5-quinquies) applies, provided that the UCI or its management company is subject to prudential supervision.
28. Art. 9(3) AIFMD Decree states that, for IRAP purposes, the provisions concerning SICAVs in arts. 3 and 6 of Decree 446 of 15 Dec. 1997 are applicable to SICAFs as well. Art. 3(2) Decree 446/97 states that all Italian UCIs are not liable to IRAP, with the exception of SICAVs. According to art. 6(4) of the same decree, the IRAP taxable base for SICAVs is determined as the difference between the subscription fees they are entitled to (*commissioni di sottoscrizione*) and the fees due to placement agents (*commissioni passive dovute a soggetti collocatori*).

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As a consequence, regulatory compliant R-UCIs are granted an extremely beneficial tax regime (the beneficial regime), which implies, in essence, that all revenues and profits generated by the real estate investments carried out by them (rents and capital gains) are exempt from income taxes in Italy.

3.2.2. Beneficial regime available to R-UCIs: Compliance with the UCI requirements and the distinction between institutional and non-institutional R-UCIs

Article 6 of Decree 351/01 states that REIFs established under article 37 of the Finance Code are not subject to IRES and IRAP. However, under the guidelines issued by the tax authorities, this rule applies only to REIFs that are in compliance with the UCI requirements set out by the Finance Code (namely the plurality of investors and the independent management of the assets).[29] Non-compliant REIFs are subject to the ordinary tax regime applicable to companies.[30]

In this respect, the tax rules[31] and the guidelines issued by the tax authorities[32] draw a distinction between institutional R-UCIs and non-institutional R-UCIs. In essence:

– institutional R-UCIs are REIFs and R-SICAFs the units/shares of which are exclusively held by one or more "institutional investors" (as defined below). These institutional R-UCIs are deemed to be in compliance with the regulatory requirements under the Finance Code and thus may take advantage of the beneficial regime[33] without the need for any further assessment as to the satisfaction of the UCI requirements; and

– non-institutional R-UCIs are REIFs and R-SICAFs where one or more participants are not "institutional investors". For non-institutional R-UCIs, compliance with the UCI requirements and, thus, the availability of the beneficial regime must be assessed on a case-by-case basis. The assessment of the compliance with the "independent management" requirement may not be straightforward in the event of non-institutional R-SICAFs (in particular when they are internally managed). Indeed, the analysis needs to take into account the specific features of a SICAF (which is a corporation, whose corporate governance rules are mainly contained in the standard Civil Code provisions) and the fact that the distinction between the management body and the shareholders/investors may not be so evident.[34]

3.2.3. Institutional investors and non-institutional investors

For purposes of the beneficial regime, "institutional investors" include the following entities:

(1) the Italian state and other Italian public entities;

(2) Italian UCIs;

(3) Italian supplementary pension schemes (*forme di previdenza complementare*) and Italian compulsory pension entities (*enti di previdenza obbligatoria*);

(4) Italian insurance companies, with limited reference to the investments designed to cover their technical reserves;

(5) Italian banks and financial intermediaries subject to regulatory supervision;

29. The Italian tax authorities have indeed stated, in a number of occasions (*see* Ruling 137/E of 4 Oct. 2005, Circular 33/E of 15 July 2011 and Circular 2/E/2012), that the tax regime for UCIs only applies to undertakings that comply with the legal and regulatory requirements (i.e. the plurality of investors and the independent management). With specific reference to the "plurality of investors" requirement, the tax authorities have clarified in the above-mentioned documents that a UCI with a sole investor can still satisfy the requirement where that investor represents itself a plurality of investors. This principle is now also stated in the rules governing R-UCIs; indeed, the beneficial regime is in any event available to institutional R-UCIs, even where their units/shares are 100% owned by one single (institutional) investor.

30. By way of background, since 2008 the Italian government and the parliament have enacted a series of new measures intended to prevent abusive applications of the favourable tax rules available to REIFs (in particular, the IRES/IRAP exemptions in art. 6 Decree 351/01 and the wider withholding tax exemption available in the past for foreign investors). Indeed, before the entry into force of these provisions, closely held and family REIFs were frequently used as vehicles to invest in real estate assets, essentially to benefit from the favourable tax rules applicable to these funds, thereby circumventing the ordinary and more cumbersome tax regime that would apply if the property were held directly by the participants. The first attempt to counteract these tax abusive practices was made in 2008 with the enactment of art. 82, paras. 17 to 22 Decree 112 of 25 June 2008, which introduced a 1% annual net worth property tax on closely held and family funds (the so-called 1% tax). The regime set out by art. 82 was repealed in 2010 by art. 32 Decree 78/2010, as subsequently amended, which reformed the regulatory and tax regime applicable to REIFs. From a regulatory perspective, art. 32 replaced the UCI definition in art. 1(1)(j) Finance Code, placing particular emphasis on the requirement that UCIs have a plurality of investors and be managed independently from them (the fine-tuning of the definition by the AIFM Decree did not change its essential features). From a tax perspective, art. 32 cancelled the 1% tax regime, restricted the withholding tax exemption for foreign investors and limited the scope of application of the IRES and IRAP exemptions to REIFs compliant with the UCI definition in the Finance Code (in this regard, *see* the government's explanatory notes to art. 32 Decree 78/2010 and Circular 2/E/2012 issued by the Italian tax authorities). Fund managers of non-compliant REIFs were required to make the necessary amendments to render the funds compliant with the Finance Code, paying a 5% lump-sum substitute tax on the REIF's net asset value as of 31 Dec. 2009. Alternatively, the fund managers had to put the non-compliant funds into liquidation and, in that event, the substitute tax rate was increased to 7%. The election between the above two alternatives (implementing the required compliance measures versus liquidation) had to be made within 30 days from the enactment by the Ministry of Economy of the regulations implementing the provisions of Decree 78/2010. However, these regulations were never enacted and art. 32 was ultimately amended by Decree 70/2011.

31. Art. 32(3) of Decree 78/2010 and para. 1 of the Regulations state that the rules in arts. 6, 8 and 9 of Decree 351/01 are in any event applicable to institutional R-UCIs.

32. *See* Circular 2/E/2012.

33. According to Circular 2/E/2012 (para. 2), "the proper tax regime of a real estate fund is applicable in any event to those funds exclusively participated by certain institutional investors". The Circular was published before the enactment of the AIFM Decree, which enacted the SICAF regime. However, the views expressed in that Circular should be applicable to R-SICAFs, as well.

34. *See* F. Mantegazza & A. Brambilla, *Implementation of the AIFM Directive in Italy – Overview of the Tax Implications*, 55 Eur. Taxn. 7, p. 294 (2015), Journals IBFD.

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(6) foreign "institutional investors", i.e. white-listed[35] states, public entities established in white-listed states and the same regulated investors listed in (2) to (5) above, provided that they are established in white-listed states;

(7) Italian mutual private entities and Italian cooperatives; and

(8) corporate or contractual vehicles (including sovereign wealth funds) that are more than 50% owned, directly or indirectly, by any of the entities listed above and established in Italy or in white-listed states.

"Non-institutional investors" are all investors in R-UCIs that do not fall within the list of "institutional investors".

The Regulations state that the notion of foreign "institutional investors" includes foreign states and public entities and other entities that (i) correspond to the Italian entities listed in (2) to (5) above and (ii) are subject to prudential supervision in their home country. The Regulations also state that the prudential supervision requirement is deemed to be satisfied when the commencement of the activity of the entity is subject to prior authorization and the entity's activities are subject to continuous mandatory controls, on the basis of the laws in force in the state of residence. Based on the Regulations, the assessment on the prudential supervision requirement must be carried out in respect of the foreign investor or in respect of the entity in charge of its management. From a documentary perspective, the Regulations point out that compliance with the prudential supervision requirement must be certified in writing by the competent foreign authorities.

The tax authorities clarified in Circular 2/E/2012 that foreign UCIs and pension funds qualify as "institutional investors" if they comply with the same substantial requirements applicable to the corresponding Italian entities (i.e. the Italian entities listed, respectively, in (2) and (3)) and pursue the same investment purposes, provided that there is a form of supervision of the fund or of the entity in charge of its management. The existence of this form of supervision must be certified in writing by the competent foreign authorities.

The primary legislation does not actually require foreign UCIs and pension funds to be subject to prudential supervision. The supervision is an additional condition imposed by the tax authorities in the Regulations and Circular 2/E/2012,[36] which also require a written statement by the competent foreign authorities confirming compliance with this requirement.

It may happen that a foreign competent authority is not in a position or available to issue the written confirmation required by the Italian tax authorities in the Regulations and in Circular 2/E/2012 in respect of foreign UCIs and pension funds. This, in the author's opinion, should not per se compromise the entity's "institutional investor" status, if the same confirmations can be gathered from other publicly available sources and documents. However, the views of the tax authorities, as expressed in Ruling 54/E/2013 and in a private ruling, seem to be more restrictive. Thus, this issue should be carefully considered.

3.3. Withholding taxes

3.3.1. Withholding tax regime applicable to investors in R-UCIs

According to article 7 of Decree 351/01,[37] a 26% withholding tax is deducted from the proceeds that result from the R-UCI's periodic statements and are distributed to the investors and, upon redemption of the units/shares, from the difference between the sale/redemption proceeds paid to the investors and the average weighted subscription or purchase price of the units/shares that are being redeemed (collectively referred to as the distributions).[38]

As a general rule,[39] the relevant Italian asset management company (i.e. the SGR) is required to deduct the withholding tax from the distributions.[40] However:

- with regard to units/shares held in a central securities depository that is managed by a duly authorized depository company, the withholding tax is deducted by the financial intermediaries with which the units/shares are deposited and which participate, whether directly or indirectly, in the central securities depository or by the non-Italian resident financial intermediaries that participate in the

35. White-listed states are those jurisdictions that allow an adequate exchange of information with Italy for tax purposes, as listed in the Decree of 4 Sept. 1996. The list was significantly broadened by the Ministerial Decree of 9 Aug. 2016 (published in the Official Gazette of 22 Aug. 2016) which added 50 additional jurisdictions (including Bermuda, the Cayman Islands, Hong Kong, Liechtenstein, Saudi Arabia and Switzerland) and grants the Italian authorities the right to remove from the list those countries that repeatedly do not comply with their exchange of information obligations. The updated white list should enter into force from the 15th day following the date on which Decree was published in the Official Gazette (i.e. 6 Sept. 2016). However, according to a different interpretation, the Decree entered into force on the same day of its publication in the Official Gazette (i.e. on 22 Aug. 2016); this view seems to be supported by the fact that on the website of the Italian tax authorities, the Decree of 9 Aug. 2016 is stated to be effective as from 22 Aug. 2016. Further clarifications from the tax authorities are therefore expected in this regard.

36. In the Regulations, reference is made to "prudential supervision". However, Circular 2/E/2012 mentions only a "form of supervision".

37. Art. 7 Decree 351/01 governs the withholding tax regime for distributions paid to investors in both REIFs and, by operation of art. 9(1) AIFMD Decree, R-SICAFs.

38. Investors are required to document the average weighted subscription or purchase price of the units/shares that are being redeemed. For this purpose, they shall provide the withholding tax agent with appropriate documentary evidence or, in the lack of supporting documents, with a written statement that certifies the amount.

39. *See* art. 7(1) Decree 351/01.

40. Art. 7(1) Decree 351/01 only contemplates distributions paid to REIFs and, accordingly, it allocates the withholding tax responsibility to the SGR. Even though art. 7(1) applies to distributions paid by R-SICAFs as well (as stated by art. 9(1) AIFMD Decree), the wording of the provision was not updated to reflect their specific features. In the event of an internally managed SICAF, there is no SGR involved and, accordingly, in the author's opinion the withholding tax responsibility should be allocated to the SICAF itself. This conclusion is consistent with the approach adopted in art. 26(quinquies) Decree 600 of 29 Sept. 1973, which governs the withholding tax regime for all other UCIs (i.e. all UCIs different from R-UCIs). Indeed, art. 26(quinquies), which was updated by the AIFMD Decree to reflect the enactment of the SICAF regime, states that the withholding tax shall be deducted by, inter alia, the SGR or the SICAF itself. In the event of an externally managed SICAF, on the opposite, the wording of art. 7(1) and 7(2-quater) Decree 351/01 suggests that the withholding tax agent should be the SGR or, as the case may be, the foreign management company.

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central securities depository or in other central securities depositories that participate in the depository where the units/shares are held;[41] ,[42]

- with regard to R-UCIs that are established and managed by a foreign management company under the freedom to provide services, this entity is required to take care of all withholding tax formalities and obligations, either directly or by appointing an Italian fiscal representative.[43]

The withholding tax is deducted from the distributions paid to all investors, regardless of their country of residence or establishment, unless one of the withholding tax reliefs considered below applies.

The withholding tax is levied as a provisional tax when the investors are companies or commercial entities tax resident in Italy (e.g. Italian banks, insurance companies and financial intermediaries). These investors must include the distributions in their IRES annual return and, possibly (depending on their status) in their IRAP annual return as well, being entitled to credit the withholding tax against their IRES liability. On the other hand, the withholding tax is levied as a final tax in respect of all other Italian taxpayers (including non-commercial entities and entities that are exempted from IRES).[44]

As an exception, no withholding tax will be levied on distributions paid to Italian supplementary pension schemes set up under Legislative Decree 252 of 5 December 2005 and Italian UCIs set up under the Finance Code.

Italian resident "non-institutional investors" owning, directly or indirectly, more than 5% of the units/shares of the R-UCI at the end of the tax period[45] are subject to the so-called "look-through tax regime" (*regime di trasparenza fiscale*), being taxed on their share of the profits realized by the R-UCI, as recorded in its periodic accounts, regardless of any distributions that may have been made.[46] ,[47] The withholding tax should, in principle, not be applicable to distributions paid to these investors. However, the assessment as to whether or not the 5% threshold is passed can be made only at year-end. Accordingly, withholding tax will, in any event, be deducted from the distributions paid to these investors, unless they refer to profits already taxed in their hands on a look-through basis in previous tax periods, being creditable against their income tax liability.

The look-through regime does not apply to foreign investors, even where they do not qualify as "institutional investors" and hold more than 5% of the units/shares of the R-UCI at the end of the tax period.[48] Distributions made to all categories of foreign investors are liable to withholding tax, at the domestic 26% rate or at a reduced rate under an applicable income tax treaty.[49],[50] By way of exception,[51] no withholding tax will be deducted from distributions paid to (i) pension funds and UCIs established in white-listed states,[52] (ii) international entities and organizations established in accordance with international agreements that are enforced in Italy and (iii) central banks and entities that also manage the official reserves of a country.[53]

3.3.2. Withholding tax regime applicable to non-Italian lenders advancing loans to R-UCIs

Under Italian rules, interest payments to foreign lenders are generally subject to a 26% withholding tax. However, new rules enacted in 2014, and subsequently amended in 2015 and 2016, provide an exemption that is available in certain specific circumstances (the

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41. *See* art. 7(2-bis/2-ter) Decree 351/01.
42. These non-Italian resident financial intermediaries are required to appoint an Italian fiscal representative for the purpose of complying with their withholding tax obligations. The fiscal representative shall pay the withholding tax to the Italian Treasury and provide the Italian tax authorities, within 15 days from their requests, with any information or documents that can provide evidence that the withholding tax obligations have been duly fulfilled.
43. *See* art. 7(2-quater) Decree 351/01, which was added by the AIFMD Decree and which makes reference to R-UCIs in general (i.e. both REIFs and R-SICAFs).
44. *See* art. 7(2) Decree 351/01.
45. For purposes of determining whether the 5% threshold is passed, both directly held units/shares and those held indirectly through controlled companies, trust companies or fiduciary persons and those owned by family members referred to in art. 5(5) Decree 917/86 (spouse, relatives up to the third degree and persons related through marriage up to the second degree) must be taken into account.
46. *See* art. 32(3-bis/4) Decree 78/2010 and the Regulations, para. 2.
47. The look-through regime implies that the profits realized by the R-UCI, as recorded in its periodic reports, are allocated to these investors, which must therefore include them in their taxable profits.
48. *See* art. 32(3-bis/4) Decree 78/2010 and the Regulations, para 2.
49. *See* art. 7(3-bis) Decree 351/01 and the Regulations, para. 2. Foreign investors that seek the application of a reduced double tax treaty rate shall deliver to the withholding tax agent the following documents: (i) a written statement from the actual beneficiary of the distributions, containing all its identification and confirming that all the conditions for the double tax treaty rate to apply are satisfied and (ii) a statement from the competent tax authorities, confirming that the beneficiary is resident in the foreign state for the purposes of the double tax treaty signed with Italy. This statement remains valid until 31 Mar. of the following year.
50. In this regard, the tax authorities clarified in Circular 2/E/2012 that reference is to be made to the interest provisions of tax treaties. Generally, tax treaties executed by Italy limit to 10% the withholding tax applicable in respect to Italian-source interest income (even though some treaties provide for a lower rate). In addition, several treaties exempt from tax in the source country interest paid to the government of the other contracting state or local authority thereof. In some cases such exemption is also extended to any agency or instrumentality (including a financial institution) wholly owned by that other contracting state or local authority thereof.
51. *See* art. 7(3) Decree 351/01.
52. As mentioned, according to the tax authorities, these are entities which, based on the relevant legal framework in the foreign country, have the same essential features of Italian pensions funds and UCIs and pursue comparable investment purposes, regardless of their legal and tax status, to the extent that a regulatory supervision is exercised over them or their management company (to be confirmed in writing, based on the Italian tax authorities guidelines, by the competent foreign supervisory body). The tax authorities also clarified in Ruling 54/E/2013 that the withholding tax exemption may also be available when qualifying pension funds or UCIs invest indirectly in an Italian R-UCI through 100% owned vehicles established in white-listed states.
53. These entities include sovereign wealth funds. According to the tax authorities (*see* Circular 2/E/2012), the exemption also applies where the sovereign wealth fund is set up in corporate form, to the extent that the foreign state owns the entire capital of the vehicle that carries out the investment in an Italian R-UCI.

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exemption). This exemption is governed by article 26(5-bis) of Decree 600 of 29 September 1973 (Decree 600/73) and applies to interest and other proceeds derived from medium- to long-term loans[54] granted to enterprises by certain qualifying lenders.[55]

As mentioned, one of the requirements for the exemption to apply is that the borrower be an Italian enterprise. This requirement seems to exclude loans granted to Italian UCIs (including therefore REIFs and R-SICAFs) from the scope of application of the exemption, as Italian UCIs do not qualify as enterprises and cannot carry out any entrepreneurial activities.

3.4. Transfer taxes

3.4.1. Registration, mortgage and cadastral taxes

As a general rule, transfers of real estate assets are subject to registration, mortgage and cadastral taxes at different rates, depending on the nature of the assets, the VAT regime applicable to the transaction and the status of the parties thereto. Real estate transactions involving R-UCIs may benefit, in some cases, from a reduction of the taxes otherwise due.

Transfers of non-residential property are generally subject to mortgage and cadastral taxes at the aggregate rate of 4%.[56] However, the aggregate rate is reduced to 2%[57] when an R-UCI is involved in the transaction (as either transferor or transferee).[58]

Contributions of a plurality of real estate assets (regardless of whether residential or non-residential) to an R-UCI, in exchange for newly issued shares or units, fall outside the scope of Italian VAT and trigger the payment of registration, mortgage and cadastral taxes at the flat amount of EUR 200 each (as opposed to the standard ad valorem rates), on condition that the majority of the contributed assets (in terms of value) are rented at the time of the contribution.[59]

3.4.2. Financial transaction tax

Italian financial transaction tax [60] is due in respect of the transfer of ownership of shares issued by Italian resident corporations[61] ' [62] and, in the case of listed shares only, an average market capitalization in November of the previous year of more than EUR 500 million. However, transfers of the ownership of UCI shares or units, including SICAVs, are specifically excluded from the scope of the financial transaction tax.[63] The explanatory memorandum on the financial transaction tax provisions clarifies that the same applies in respect of units in exchange-traded funds.

On the basis of the above, no financial transaction tax should be due on the transfer of REIF units or R-SICAF shares. This is clearly the case for REIF units. The same conclusions should be drawn in the case of R-SICAF shares, which, in principle, could fall within the

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54. Even though the rules are silent on this point, it is generally believed, on the basis of other Italian tax provisions concerning medium- to long-term loans, that these are loans with a maturity in excess of 18 months.
55. According to the original wording of this provision, as enacted by Decree 91 of 24 June 2014 (Decree 91), the exemption was available in respect of interest and other proceeds derived from medium- to long-term loans granted to enterprises by (i) credit institutions established in an EU Member State, (ii) insurance companies established and authorized under the laws of an EU Member State, (iii) unleveraged collective investment undertakings, even if not subject to tax, established in an EU Member State or in a white-listed states part of the EEA. The wording in Decree 91 excluded from the scope of application of the exemption a large number of international debt providers, namely all institutional investors that did not qualify as "collective investment undertakings", the collective investment undertakings that made recourse to financial leverage or were established outside the EU/EEA. Art. 26(5-bis) was amended by Decree 3 of 24 Jan. 2015 (Decree 3/2015), which broadened the scope of application of the exemption, making it available to a larger number of foreign institutional investors. Under the new rules, in fact, the exemption applies to interest and other proceeds derived from medium- to long-term loans granted to Italian enterprises by the following qualifying foreign lenders:

    (1) credit institutions established in EU Member States. The exemption should be available to both EU resident banks and non-EU resident banks (e.g. US banks) acting through an EU permanent establishment;

    (2) entities under art. 2(5)(4) to 2(5)(23) Directive 2013/36/EU. These are development promotion institutions established in different EU Member States;

    (3) insurance companies incorporated and authorized under provisions enacted by EU Member States; and

    (4) foreign institutional investors under art. 6(1)(b) Legislative Decree 239/96, even if not liable to tax, that are subject to forms of supervision in their State of formation. These are entities which, regardless of their legal or tax status in their home country, have as their principal activity that of managing investments on their own account or on behalf of third parties, such as insurance companies, investment companies, investment funds, SICAVs and pension funds.

    The Decree 18 of 14 Feb. 2016 slightly amended the wording of art. 26(5-bis), stating that the exemption applies without prejudice to the rules in the Finance Code concerning lending to the public as a restricted activity.
56. 3% mortgage tax and 1% cadastral tax.
57. 1.5% mortgage tax and 0.5% cadastral tax.
58. *See* art. 35(10-ter) Law Decree 223 of 4 July 2006, which applies to both REIFs and, by provision of art. 9(1) AIFMD Decree, R-SICAFs.
59. *See* art. 8(1-bis) Decree 351/01 (which applies to both REIFs and, by provision of art. 9(1) AIFMD Decree, R-SICAFs) and the guidelines of the Italian tax authorities in Circular 22/E of 19 June 2006.
60. The financial transaction tax was introduced by art. 1, para. 491 to 500 Law 228 of 24 Dec. 2012 (*Legge di Stabilità 2013*, the Stability Law), which was published in the Official Gazette on 29 Dec. 2012. The tax is also governed by the implementing provisions enacted by the Treasury (Decree of 21 Feb. 2013, as subsequently amended in Mar. and Sept. 2013; the Treasury Decree) and by the payment and reporting regulations enacted by the tax authorities in July 2013.
61. Art. 1(2)(c) of the Treasury Decree defines "shares" as follows: "stocks of companies belonging to one of the following types, even if falling into a special category, and regardless of the assignment of certain administrative or property rights: companies under Italian law known as '*società per azioni*', '*società in accomandita per azioni*' and European companies referred to in Regulation (EC) 157/2001, as well as stakes of companies under Italian law known as '*società cooperative*' and '*mutue assicuratrici*', unless the articles of incorporation stipulate that the laws for companies under Italian law known as '*società a responsabilità limitata*' pursuant to article 2519, paragraph 2 of the Italian Civil Code, should apply".
62. The residence of a company for financial transaction tax purposes is the place where the entity has its registered office (meaning its official corporate seat or *sede legale*).
63. *See* art. 2(2) Treasury Decree.

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notion of "shares" for financial transaction tax purposes.[64] Indeed, on the hand, R-SICAFs qualify as UCIs and transfers of the ownership UCI shares are outside the scope;[65] on the other hand, the rules clearly state that SICAV shares are not chargeable equities for financial transaction tax purposes, and there would be no logic in adopting a different approach for SICAFs.

3.5. Anti-avoidance and beneficial ownership

The availability of the tax reliefs that are available for investments in Italian R-UCIs, as discussed above, is subject to anti-avoidance and beneficial ownership tests.

3.5.1. Anti-avoidance rule

Article 1 of Decree 128 of 5 August 2015 has brought about a new general anti-avoidance rule (GAAR) within the Taxpayer Bill of Rights (Law 212/2000), with a view to providing more certainty to taxpayers. The GAAR replaces and supplements the previous (semi-general) anti-avoidance provision under article 37-bis of Decree 600/73[66] and the abuse-of-law doctrine developed by the Supreme Court,[67] which has been extensively applied by the Italian tax authorities and tax courts beyond the narrow borders governed by article 37-bis.

An abuse of law exists when one or more transactions "lack any economic substance and, despite being formally in compliance with tax laws, are essentially aimed at obtaining undue tax advantages". These abusive schemes are not enforceable toward the tax authorities, which will disregard the tax advantages so achieved and compute the taxes on the basis of the rules and principles that have been circumvented, taking into account any tax payments made by the taxpayer in connection with the abusive transactions.

The GAAR specifically states that transactions are deemed to lack any economic substance when they consist of facts, acts and contracts – even interconnected – that are not suitable to generate economic effects different from the tax advantages. The inconsistency between the individual transactions and the underlying rationale of their aggregation, or between the legal instruments that have been adopted and common market practices, can be regarded as evidences of a lack of economic substance.

The undue tax advantages that may be challenged under the GAAR consist of benefits, even if not achieved in the short term, that are in conflict with the purpose of the tax provisions or with the principles of the tax legal framework.

There is no abuse when a transaction is justified by sound and non-marginal non-tax reasons, including managerial and organizational reasons aimed at improving the structure or functionality of the business.

Taxpayers are allowed to choose between different optional tax regimes provided by the law or between alternative transactions leading to a different tax burden. In other words, it is recognized that under Italy's detailed rules, taxpayers frequently have a choice as to the manner in which transactions can be carried out, and that different tax results arise depending on the choice that is made. The GAAR does not challenge such choices. It may, however still apply if the course of action taken by the taxpayer cannot be regarded as reasonable and essentially aims to achieve a favourable tax result that the parliament did not anticipate when it introduced the tax rules in question.

The GAAR also sets out the formalities that must be followed for abuse of law tax assessments, and specifically states that abuse of law does not amount to a tax crime.

3.5.2. Beneficial ownership

The beneficial ownership test (generally in combination with the anti-avoidance test) is relevant for tax reliefs that may be available in respect of distributions and capital gains. No specific beneficial ownership definition is available under Italian tax rules, except for the provisions implementing the Interest and Royalties Directive, where it is stated that foreign associated companies receiving Italian-source interest or royalties are deemed to be beneficial owners if they receive such payments as final beneficiaries and not as intermediaries (i.e. acting as agents or nominees).

In general terms, the beneficial owner is the person who has the "availability" of the relevant income. In this regard, an intermediate holding company with no substance and acting as a conduit entity between an Italian R-UCI and the ultimate investor(s) may generally not pass the beneficial ownership (and anti-avoidance) tests, as confirmed by the Italian tax authorities on a number of occasions, including the recent guidelines on leveraged acquisitions.[68] However, with specific reference to R-UCIs, the Italian tax authorities have acknowledged that certain foreign investors that are granted a withholding tax relief (e.g. foreign pension funds and UCIs) may carry out the investment through (a chain of) 100%-owned vehicles.[69] In these cases, therefore, the availability of the withholding tax relief should reasonably not be disregarded on beneficial ownership/anti-avoidance grounds.

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64. *See supra* n. 61.
65. *See supra* n. 63.
66. The scope of application of art. 37-bis was limited to Italian income taxes and to a closed list of transactions.
67. According to the Supreme Court, prohibition of abuse of law is a general, unwritten principle which stems from the Italian Constitution and from the EU Directives.
68. Circular 6/E/2016 published on 30 Mar. 2016.
69. *See supra* n. 52.

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