

20 December 2022

Investment management exemption for certain investment funds to be introduced effective from 1 January 2023

Article 49 of the bill of 2023 Financial Law, which must be approved within 31 December 2022, to be effective from 1 January 2023, introduces the so called “Investment Management Exemption” in the Italian tax system

Background

If approved, Article 49 will amend the definition of permanent establishment (PE) under Italian law, clarifying that an entity operating in Italy in the name and on behalf of a “foreign investment vehicle”, or of its controlled entities, habitually concluding, or in any way contributing to the conclusion of, purchase, sale and/or trading contracts of financial instruments (including derivatives, equity participations and credits) does not amount to an Italian PE of the foreign investment vehicle, even if it exercises discretionary powers, if the following conditions are met:

- 1) the foreign investment vehicle and its controlled companies are located or established in a white-list country (i.e., in a country allowing a satisfactory exchange of information with Italy, listed in the Ministerial Decree of 4 September 1996);
- 2) the foreign investment vehicle complies with certain independency conditions, which will be identified by a Ministerial Decree;
- 3) the entity carrying out the activities on behalf of the foreign investment entity:
 - a. does not seat in any management or supervisory body of the foreign investment vehicle and any of its (directly or indirectly) subsidiaries;
 - b. is not entitled to more than 25% of the economic results of the foreign investment vehicle, including profit participations to other companies of the same group (a ministerial decree shall detail the criteria to compute this 25%), and
- 4) the entity carrying out the activities on behalf of the foreign investment entity is remunerated at arm’s length for services rendered to other group companies, and such remuneration is duly allocated to the activities carried out in Italy and documented by specific transfer pricing documentation. The Italian tax authorities shall provide further guidance on the arm’s length remuneration.

Preliminary comments

The current draft of the provision does not stand out for clarity, since it seems to refer to PEs of foreign private equity / debt funds and of their controlled investment vehicles, while apparently it does not cover possible PE issues related to investment management companies and advisory companies.

In addition, while the investment in financial instruments and credits is expressly considered, other types of investments (including real estate ones) are excluded.

Last, it's not clear to which type of financial activities it applies, whether only to trading or also to other management activities (including, for example, active management of shares and other financial instruments).

Notwithstanding the above, the introduction of the Investment Management Exemption in the Italian Income Tax Code might be a first step forward to eventually provide much clarity and comfort to (certain) investment management companies operating in Italy on a cross-border basis, especially if amended to clearly broaden its scope to management and advisory companies (and possibly smoothen the conditions to limit them to the maximum extent possible).

Investment management companies and their affiliates should assess whether their current or perspective operations in Italy would fall within the scope of application of the new piece of law, and therefore exclude any kind of PE issues with reference to the funds and their controlled companies, holding or making Italian investments.

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