

Financial activities carried out by EU Funds

The Bank of Italy recently approved and published in the Official Gazette¹ a set of rules amending the Regulation on collective investment management of 19 January 2015² (the “**Regulation**”), concerning, among other things, the authorization of EU alternative investment funds (“**AIFs**”) to directly provide loans in Italy.

These new rules constitute the final step, in Italy, in the construction of a comprehensive legislative framework allowing direct financing from investment funds established in the European Union and implement the provisions of article 46-*ter et seq.* of the Italian Financial Act³. As a consequence, EU AIFs, alongside Italian AIFs, are now expressly allowed to provide direct lending to entities other than consumers in Italy.

For such activity to be carried out, however, the following conditions must be met (“**Conditions**”):

- i. the EU AIF must be authorized by the competent authority to carry out lending activities (including direct lending) in the country of origin;
- ii. the EU AIF must be a closed-end entity and have a functioning/governing model - with particular reference to rules regarding purchase/holding of units - similar to that of Italian AIFs that carry out direct lending;
- iii. the regulations and standards of the country of origin relating to the limits and risk management (including limitations on the use of leverage) must be equivalent to the standards governing Italian AIFs that carry on direct lending. The requirement of equivalence can also be met by reference to the by-laws or regulatory provisions of the EU AIF, as long as the competent authority of the home jurisdiction ensures compliance with them.

The ability to carry out lending activities in Italy by EU AIFs is subject to an authorisation procedure involving the Bank of Italy, which is in charge of assessing whether all necessary Conditions are met by the applicant.

More specifically, for the purposes of obtaining the authorisation, the Italian Financial Act and the Regulation (as recently amended), require, among other things, the delivery by the EU AIF of a prior notice (“**Notice**”) which must contain comprehensive information about the applicant EU AIF and its fund manager, and to which a number of documents must be attached, including the following:

1. a declaration from the competent authority of the home country, confirming that the fund manager is duly licensed for fund managing activities or, as an alternative, a copy of the licensing documents together with a certificate from a legal representative of the fund;
2. a declaration by the competent authority in the home country or, alternatively, a legal opinion, certifying that the relevant EU AIF is authorised to carry out lending activity in its home country;

¹ *Gazzetta Ufficiale della Repubblica Italiana*

² *Regolamento sulla gestione collettiva del risparmio*

³ Legislative Decree No. 58 of 24 February 1998

3. a declaration of a legal representative of the EU AIF manager identifying the legal provisions that are binding on the EU AIF in the home country referred to under point iii. above (a copy of which must be attached to the declaration) deemed to be equivalent to the corresponding Italian legal provisions, and a legal opinion certifying this equivalence; or
4. as an alternative to the declaration provided for under point 3. above, a declaration by the competent authority in the home country confirming that said authority will monitor the enforcement by the relevant EU AIF manager of the provisions of the by-laws or the internal regulation of the EU AIF referred to under point iii. above; and
5. constitutional documents of the EU AIF, a note about the functioning of the AIF and latest available fund management reports.

The Notice must be served by the EU AIF on the Bank of Italy at least 60 days before it intends to start its lending activities. The Bank of Italy may request supplemental information if the Notice is deemed incomplete or, if not, will serve a delivery receipt (*comunicazione di ricezione*). If any of the Conditions are not met, the Bank of Italy may prohibit the applicant EU AIF from starting lending activities in Italy within 60 days from the date of the above delivery receipt. If the term lapses without any prohibition being issued, lending activities can start.

While lending activities are being carried on, the fund manager must send the Bank of Italy any fund reports within 10 days from their respective approval. In addition, any modification to the data and information provided in the context of the authorisation procedure must be provided to the Bank of Italy which, in turn, assesses whether the relevant EU AIF can continue its lending activities in Italy.

From an operational standpoint, the managers of an EU AIF operating in Italy will be subject to the legislation on transparency and relationships with customers provided for Italian operators, except for the provisions relating to compulsory adherence to the out-of-court dispute resolution system provided for under the Italian Banking Act⁴, as well as the supervision by Consob and Bank of Italy. Lastly, the fund manager of an EU AIF must ensure compliance with Italian regulatory requirements.

Tax regime

EU AIFs directly lending to Italian companies are exempt from any withholding tax on payment of interest and similar income from Italian borrowers, so long as the following conditions are met:

- i. they comply with the regulatory provisions regarding lending to the public (including the Conditions mentioned above);
- ii. the financing qualifies as a medium-long term loan. The relevant provision does not define what a medium-long term loan is, however, under the banking regulations, this means a loan having a maturity longer than 18 months. In contrast, a certain interpretation of the substitute tax under article 15 of Presidential Decree 601/73 (see below) makes reference to a maturity longer than 18 months and one day;
- iii. the money is advanced to Italian entities carrying on a business activity (the relevant law refers to “*imprese*”);

⁴ art. 128-bis of Legislative Decree No. 385 of 1 September 1993

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It does not constitute a reference for agreements and/or commitments of any nature.

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- iv. the EU AIF is beneficially entitled to the income and qualifies as an institutional investor subject to supervision (*vigilanza*) in its country of establishment⁵; for these purposes, the definition of “institutional investor” would include EU AIFs duly authorized to carry out direct lending in Italy and subject to supervision in their country of establishment.

If the conditions for the exemption are not met, a final 26% withholding tax (or the lower rate provided for by double tax treaties concluded with Italy, if applicable) is levied on interest and other proceeds paid out of loans and other financing provided to Italian resident entities.

Loans executed in Italy by EU AIFs can benefit, on the option of the parties, from the 0.25% substitute tax regime regulated by article 15 and ff. of Presidential Decree 601/73; to access the preferential regime, the relevant loan agreements must provide for a maturity longer than 18 months (this minimum maturity has been interpreted as being met where the term is longer than 18 months and one day).

If the option is validly exercised, any stamp duty, registration tax, mortgage or cadastral tax and other governmental taxes which would ordinarily apply to the financing and any documents and formalities connected thereto (including the securities and guarantees comprising the security package), are replaced by the 0.25% substitute tax, which is levied on the amount made available in connection with the facilities.

⁵ The relevant country needs to be listed in the so called white list set out in Ministerial Decree of 4 September 1996, which includes EU countries