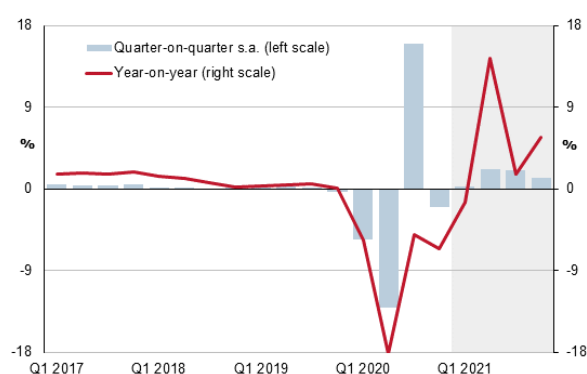


## Doing Business in Italy

Last reviewed - February 2021

### Italian Economic Data



In Q4, GDP fell 2.0% over the previous quarter in seasonally- and working-day adjusted terms. The result sharply contrasted Q3's historic 16.0% quarter-on-quarter rebound and was broadly in line with market expectations of a 2.2% drop. The economy swung back into contraction as tighter restrictions were introduced in October-November and were further intensified over the Christmas period. Meanwhile, in annual terms, the economy shrank 6.6% in Q4, worsening from the 5.1% contraction recorded in Q3. Taking the year, GDP plunged a record 8.9% in 2020, contrasting 2019's anemic 0.3% increase.

Q4's reading reflected decreased output in all sectors—primary, industry and services—as lockdown measures weighed on business activity and consumer spending. On the demand side, preliminary data indicates that both domestic and external demand made negative contributions to growth.

Turning to this year, GDP should recover some of last year's losses as the gradual easing of restrictions and rising inflows of EU funds unleash pent-up capital and consumer spending, and the reopening of economies abroad fuels external demand. That said, the pandemic has dealt a severe blow to Italy's already-ailing economy and has led to a widening of the fiscal deficit and further accumulation of the mountainous stock of public debt, while also deteriorating banks' balance sheets. EU recovery funds should reduce the likelihood of financial turmoil, although political instability and long-standing problems such as a cumbersome public sector, much-needed market-friendly reforms, high taxes and a sluggish judiciary all cloud the outlook for Italy's economy.

|            |  |
|------------|--|
| Population | Decrease 60,244,639 (1 January 2020 provisional) |
| GDP        | Decrease \$1.8 trillion                          |
| GDP rank   | 8th (nominal, 2020), 12th (PPP, 2020)            |
| GDP growth | +0.8% (2018)                                     |
|            | +0.3% (2019)                                     |

GDP by sector :  
agriculture: 2.1%  
industry: 23.9%  
services: 73.9%

Inflation (CPI) :  
0.1% (2020 est.)  
0.6% (2019)  
1.2% (2018)

Human Development Index  
Increase 0.892 very high (2019) (29th)  
Increase 0.783 high IHDI (2019)

Unemployment  
Positive decrease 9.0% (December 2020)  
Negative increase 31.1% youth unemployment (15- to 24-year-olds; July 2020)  
Positive decrease 2.1 million unemployed (Q2 2020)  
Average gross salary €2,446 / \$2,740 monthly (2019)  
Average net salary €1,729 / \$1,936 monthly (2019)

Main industries  
Tourism, machinery robots, agriculture, aircraft electronics defense systems, iron and steel, chemicals, food processing, pharmaceutical, textiles, motor vehicles, clothing foot wear, ceramics, cruise ship, electric power

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## Corporate - Taxes on corporate income

### Applicable rates

Italian corporate entities are subject to a corporate income tax, known as *imposta sul reddito sulle società* or IRES, and to a regional production tax, known as *imposta regionale sulle attività produttive* or IRAP.

The standard rates are as follows:

- 24% for IRES.
- 3.9% for IRAP.

Up to FY 2016, the IRES rate was 27.5%. Specific rules apply for bank and financial entities. Different IRAP rates are applicable for certain entities (i.e., banks and financial entities, insurance corporations, entities with a determined governmental exclusive right to provide services). Regions have the power to slightly increase or decrease IRAP rates.

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## General rules

### IRES

The IRES taxable base is determined according to the worldwide taxation principle, which states that, regardless of the location/jurisdiction where the income is produced, to the extent that the income is legally attributable to an Italian resident entity, the income is taxed in Italy. IRES is charged on the total net income reported in the financial statements of the company as adjusted for specific tax rules. Non-resident companies are taxed only on Italian-source income.

### IRAP

There are different methods of computation for the IRAP taxable base, depending on the nature of the business carried out by the taxpayer. Provisions for liabilities and risks, as well as extraordinary items, cannot be considered when determining the IRAP taxable base.

For sales and manufacturing companies, the IRAP taxable base is broadly represented by the company's gross margin in its financial statements. In addition to the non-deductible items mentioned above, interest income and expense and provisions for bad debts are excluded for the purposes of the IRAP taxable base.

For banks, the IRAP taxable base is broadly defined as follows:

- Intermediation margin reduced by 50% of dividends.
- 90% of amortization costs relating to fixed tangible and intangible assets.
- 90% of other administrative expenses.
- Net value of adjustments and reassessments for bad debts.

Special rules apply to financial institutions, other than banks, and holding companies.

IRAP is levied on a regional basis, and regions can increase or decrease the standard IRAP rate up to 0.92%. Companies with facilities in different regions must allocate their overall taxable base to the different regions based on the employment costs of personnel located at the various sites. Facilities become relevant to the calculation of IRAP if they have been established for more than three months. Italian companies with permanent establishments (PEs) abroad, as well as shipping companies qualifying for the tonnage tax regime (*see Tonnage tax below*), are not subject to IRAP on the income earned through these PEs.

The deduction of labour costs for IRAP purposes depends on the type of hiring contract. In particular:

- Full deduction for costs related to employees hired with an open-ended contract.
- Deduction limited to contributions for compulsory insurance against accidents (i.e. *Istituto Nazionale Infortuni sul Lavoro* or INAIL) for temporary employees.

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### **Substitutive tax on reorganizations (mergers, de-mergers, contributions in kind)**

Corporate restructurings, such as mergers, de-mergers, and contributions in kind, are, in principle, tax neutral even if, for financial accounting purposes, the transaction results in the recognition of higher values of the assets or of goodwill. Companies may elect to obtain partial or full recognition for tax purposes of the step-up in the financial accounting values of assets or of the goodwill arising from the corporate restructurings, provided they pay a substitutive tax.

The substitutive tax is calculated on the step-up in tax basis and is based on progressive rates of 12% to 16% (i.e., 12% up to 5 million euros [EUR], 14% from EUR 5 million to EUR 10 million, and 16% over EUR 10 million) to be paid by the deadline of the tax payment of the fiscal year in which the reorganization took place or the following fiscal year. The substitutive tax may also be paid in three annual instalments of 30% in the year of election, 40% in year two, and 30% in year three plus interest at the rate of 2.5% per year on the deferred amounts. The substitutive tax is not deductible for the purposes of IRES or IRAP.

In addition, stepped-up values of goodwill and trademarks acquired from the reorganization transactions carried out since 1 January 2016 may be depreciated for tax purposes over five tax years, instead of 18 years, by paying a substitutive tax of 16%. Substitute tax needs to be paid by the deadline of the tax payment of the fiscal year in which the reorganization took place. Payment in instalments is not allowed. The higher tax depreciation arising from this election is effective from the tax period subsequent to the one in which the substitutive tax is paid. For example, if a merger transaction occurred in year one and the substitutive tax was paid in year two, the increased tax depreciation would begin in year three.

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### **Free step up on reorganizations (mergers, de-mergers, contributions in kind)**

Under certain conditions a free step-up of the tax basis of capital assets in case of mergers, demerger and contributions in kind is granted up to Euro 5 million. The law provides for a free tax step-up regime for both corporate and regional tax purposes for companies receiving assets upon mergers, de-merger or contributions in kind which take place between May 1st, 2019 and December 31, 2022. That means that the increased accounting value of goodwill, tangible and intangible assets accounted for by the receiving entity will be recognized for tax purposes. The benefit applies to mergers, de-mergers and contributions in kind which occur between companies not belonging to the same group and under the condition that such entities carried out their business activity for at least 2 years.

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### **Tonnage tax**

Italian tax resident shipping companies, as well as non-resident shipping companies operating in Italy through a PE, can qualify for and then elect to be subject to the Italian tonnage tax regime. The regime basically allows for the determination of presumptive income based on the net tonnage of the qualifying ships apportioned to the effective shipping days (tonnage income). The tonnage income is subject to IRES only.

To qualify for the tonnage tax, ships must: (i) have a net tonnage of more than 100 net tons (NT); (ii) be used for goods transportation, passenger transportation, salvage, towing, and other services; and (iii) operate in international shipping as defined by the rules disciplining Italian International Registry. Ships chartered out on a bare boat charter are excluded. Chartered ships with crew are

included in the tonnage tax regime if their global net tonnage is less than 50% of the total net tonnage.

Tonnage income is calculated based on the ship's net tonnage.

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### **Italy and VAT registration by UK businesses (post-Brexit)**

The Italian tax authority concluded that under the free trade agreement between the EU and the UK, (signed 24 December 2020 and provisionally in force as of 1 January 2021), UK businesses and companies can directly register for value added tax (VAT) in Italy.

Guidance (Resolution no. 7 of 1 February 2021) from the Italian tax authority clarifies that:

- UK businesses or companies without an Italian VAT number can register in Italy for VAT purposes either (1) directly or (2) through the appointment of a fiscal representative.
- UK businesses that were previously directly registered for VAT in Italy can continue doing business in Italy through this direct VAT registration (without having to switch to the fiscal representative registration). Thus, the input VAT incurred by these businesses after 1 January 2021 is recoverable via their direct VAT registration with no risk of challenges or penalties.
- UK businesses that were previously VAT-registered in Italy by means of the appointment of a fiscal representative can continue doing business in Italy in the same manner.

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