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LAW DECREE 3/2015 COMPLETES THE PICTURE OF LAW DECREE 91/2014 TO RESHAPE REGULATION FOR INDIRECT LENDING IN ITALY

On January 24, 2015, Law Decree n. 3/2015 has been published on the Official Journal of the Republic of Italy. It is aimed to introduce several new rules to stimulate Italian economy and attracting foreign investments, by removing certain hindrances and introducing tax incentives for indirect lending. Among many provisions touching upon different areas of law, the law Decree enlarges the scope of certain provisions of Law Decree no. 91 of 24 June 2014 on indirect lending ultimately deregulating it. The Decree is effective from 25 January 2015. It now has to be converted into law by Parliament within 60 days. Amendments to the Decree could be passed during the conversion process.

The main provision of Law Decree 3/2015 touches upon: (i) direct lending to exporters by Italian ECA SACE, (ii) special regime for innovative SMEs, (iii) special tax incentives for patents and trademarks, (iv) additional sources for financing for SMEs, (v) tax regime of medium-long term financing when provided by foreign lenders.

As far as foreign investors are concerned, the main provision of Law Decree 3/2015 is article 6, whereby the number of entities eligible for exemption from the withholding tax on interest paid on medium-long term facilities is significantly increased. The new provision is of remarkable interest for foreign investment funds and completes the process of tax exemptions and facilitations for those entities started by Law Decree 91/2014.

Withholding Tax Exemption on Interest on Medium-Long Term Facilities

Particularly, article 6 of Law Decree 3/2015 now extends that withholding tax exemption to all foreign institutional investors, irrespective of their legal structure and their recourse to financial leverage.

By way of background, under Italian tax rules, interest paid on loans is generally subject to a 26% withholding tax (20% for interest accrued until July 1, 2014). Section 22 of Law Decree 91/2014 introduced an exemption from such withholding tax for interest paid by Italian borrowers on loans that are Medium-Long Term Debt to the following foreign categories of creditors: (i) financial institutions established in a EU Member State, (ii) insurance companies established and authorized under the law of a EU Member State, (iii) collective investment undertakings not using financial leverage. The wording used by Law Decree 91/2014 made clear that the withholding tax exemption was not applicable to a large number of international debt providers, namely those institutional investors that were not qualified as "collective investment undertakings" and/or to those that makes recourse to financial leverage.

Law Decree 3/2015 now broadens the definition of investors under (iii) above and aligns the Italian regulation to the regulation of other European countries, making Italian companies as attractive to international funds as their European competitors.



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As mentioned, this new rule is in the context of a wider process of tax facilitations for foreign debt provider. In addition to the withholding tax exemption on interest earned on medium-long term facilities, these investors can now benefit from: (a) the withholding tax exemption on interest on non-listed securities, set out by section 21 of Law Decree 91/2014 and (b) the Substitute Tax regime set out by section 22 of Law Decree 91/2014.

(a) Withholding Tax Exemption on Interest on Non-listed Debt Securities

Under Italian tax rules, interest paid on debt securities are generally subject to a 26% substitute tax (20% for interest accrued until July 1, 2014). Under previous tax law, interest earned on any debt securities issued by banks and listed corporations and listed debt securities issued by any other entities were exempt from such substitute tax provided that (i) the beneficial holders of such securities are resident in White Listed Countries and (ii) such holders comply with certain standard certification procedures. Law Decree 91/2014 extends this exemption to non-listed debt securities issued by non-listed issuers so long as they are held only by qualified investors. Furthermore, the Decree also contemplated that in the event that the co-investors in the debt securities described above are both EU collective investment undertakings and/or Securitization SPVs and other investors that do not qualify as qualified investors, such exemption on interest paid to EU collective investment undertakings and/or Securitization SPVs applies provided that (i) more than 50% of their assets consist of the debt securities mentioned above and (ii) their investors are solely qualified investors

(b) Substitute Tax

The Substitute Tax is an optional regime that, before Law Decree 91/2014, applied to bond issuances having a maturity longer than eighteen months and to loans, and their relating security package, (i) extended by qualified financial institutions, (ii) having a maturity exceeding eighteen months, and (iii) executed in Italy, in lieu of all transactional taxes ordinarily applicable thereto. Whenever the ordinary regime would entail a transactional tax cost in excess of 25 bps, *i.e.* the rate at which the substitute tax is currently applicable, the Substitute Tax is clearly advantageous. Otherwise (*i.e.* whenever the loan/bonds issuance and related security package would be subject to nominal taxes), the substitute tax would ultimately result in an increased cost of the financing. The optionality of Substitute Tax enables the borrower to choose and, hence, to assess in advance whether such regime is in fact advantageous

Until Law Decree 91/2014, the Substitute Tax option was only available if the lender was an Italian bank regulated under the Italian Banking Act, an Italian authorized permanent establishment of a foreign bank, EU or non-EU, an EU bank or the financing was in the form of a bond. Law Decree 91/2014 has broadened the list of entities eligible for such Substitute Tax by including securitization SPVs, insurance companies and collective investments undertakings established in a EU Member State or in a European Economic Area "White List" State. Moreover, the Decree broadens the Substitute Tax Regime's to transfers of the participation in the financing that benefited from the regime, of the relating receivables and related security interest (see Article 22, paragraph 2, of Law Decree 91/2014).

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Studio Legale Padovan has broad experience in the field of asset based lending, re-financing transactions, leasing, factoring, assets-backed/securitization transactions, on-demand bank guarantees, export credits, syndicated loans and related security arrangements. The lawyers of the Firm regularly advise institutional investors on compliance and reporting requirements to the Bank of Italy and other regulatory authorities.

The Firm is active in the field of securities transactions and assists its clients in all the contractual, corporate and regulatory matters relating to the issuance and placement of shares, bonds and warrants. The Firm has represented institutional clients in a number of innovative securitization deals.

The Firm specializes in all aspects of the operation of domestic and foreign funds and investment companies, including the placement in Italy of units of EU and non EU vehicles.

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