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News Analysis: Italy's Proposed Financial Transaction Tax

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NEWS ANALYSIS

Italy's Proposed Financial Transaction Tax

by Gaetano Pizzitola, Roberto Munno, Giovanni Ricco, and Antonio Vicentini

As two opposing EU blocs debate the feasibility of an EU-wide financial transaction tax (FTT), the Italian government wants to accelerate the introduction of its own proposed FTT. (For prior coverage, see *Tax Notes Int'l*, Oct. 29, 2012, p. 452, *Doc 2012-21932*, or *2012 WTD 206-2*.)

Indeed, the government's proposal, although with a different shape and scope, is reminiscent of a previous FTT, the so-called *fissato bollato*, that was introduced in the 1920s and abolished in 2008, after going through various amendments that had progressively restricted its scope. The proposed new FTT has a wider scope, also applying to derivative transactions.

Following is an outline of the government's proposal as initially presented. Significant changes are expected, however, before the proposal becomes law. We have also provided an unofficial translation of the draft language in the proposal.

The Proposal

The FTT legislative framework is under article 12, paragraphs 18-21, of the draft Stability Law, a package of austerity tax measures proposed as part of the government's fiscal stability program for 2012. (At the time this article was written, the Stability Law still had to be approved by the Chamber of Deputies before passing to the Senate for a second review and vote.)

About €1.1 billion in incremental annual tax collections have been budgeted based on the proposed FTT framework, factoring in a potential reduction in the volume of financial transactions, particularly on derivatives.

Effective Date

The FTT is intended to take effect on January 1, 2013. However, the effective date depends on the final version of the Stability Law approved by the Parliament as well as the implementing regulations, which should be published within 60 days from the entry into force of the Stability Law.

Meanwhile, temporary tax relief and FTT deferrals may be expected even if the January 2013 start date is not postponed. In light of issues raised by intermediaries about the need to update their software to adapt to the new FTT, the Italian Banking Association (ABI) has proposed an amendment to postpone the date on which intermediaries are required to remit FTT to the Revenue Agency.

Applicable Transactions

As proposed, the FTT would apply to two main classes of transactions: sales of shares and assimilated financial instruments issued by Italian resident entities, and derivatives.

Sales of shares and assimilated instruments would be subject to FTT regardless of whether they are listed or are privately held, as clarified by the government's illustrative notes to article 12, paragraph 18, of the Stability Law.

Assimilated instruments, as defined in the Stability Law, are participating financial instruments, including preferred shares.

Quotas issued by limited liability companies such as the Italian Srl should not be within the scope of FTT, although this is not crystal clear at this stage. Sale of partnership interests should also be exempted from the FTT. Indeed, the application of the FTT to sales of Srl quotas and partnership interests seems to go beyond the objective of the FTT, which is to target trading on shares and derivatives, which ordinarily occurs much more frequently than sales of Srls and partnerships, the latter ordinarily being tailored to long-term investments.

As a rule, bonds should not be subject to FTT even if they are convertible into shares. It is doubtful that profit-participating bonds will be assimilated to shares, thereby becoming subject to FTT. The issuance and redemption of shares and assimilated instruments also are excluded from the FTT.

Derivatives would generally be subject to the FTT, with the exception of derivatives on treasury bonds issued by EU member states and European Economic Area countries with qualifying exchange of information mechanisms between their competent authorities.

Derivatives also would be subject to FTT regardless of whether they are speculative or are for hedging purposes. This is one aspect of the draft law that has come under major criticism.

Territoriality and Subjective Scope

As a rule, transactions within the objective scope of FTT would actually be subject to tax only if one of the two counterparties is an Italian resident. However, sales of shares and assimilated instruments between two nonresident taxpayers would also be subject to FTT if executed in Italy (for example, through an Italian office of a bank or other intermediary or notary).

In other words, derivatives transactions would be subject to FTT only if one of the two parties is an Italian resident, whereas transactions involving shares and assimilated instruments would be subject to tax only if those instruments are issued by Italian resident companies in one of the following two scenarios:

- transactions between two nonresident taxpayers (taxable only if executed in Italy); or
- transactions between an Italian resident taxpayer (either seller or purchaser) and a nonresident, or between two Italian resident taxpayers (taxable in all circumstances, whether executed in Italy or abroad).

This system has been criticized for potentially discouraging the trading of shares in Italy between two nonresident parties, while increasing transaction costs for Italian resident investors only. The ABI has proposed extending the territorial scope of the FTT to all transactions involving shares issued by Italian companies, executed either in Italy or abroad, regardless of the residency of the counterparties.

Tax Base

Under the current proposal, the tax base for transactions involving shares and assimilated instruments would be based on the transaction ''value.'' The language of the draft law is not clear whether the consideration paid by the purchaser to the seller would be characterized as the transaction value and treated accordingly.

Intragroup transactions likely would be subject to transfer pricing scrutiny (the arm's-length test), although they should be excluded from the FTT, based on its objectives.

The tax base on derivative transactions would be their notional value.

Tax Rate

Under the proposal, the same 0.05 percent rate would apply on both classes of transactions (that is, whether they involve shares and assimilated transactions or derivatives).

Derivatives would be subject to tax on the basis of their notional value — another aspect of the draft law that has drawn criticism — and as a result, the derivatives tax rate is expected to decrease. In particular, the ABI has proposed a 0.02 percent tax rate for derivatives transactions.

Persons Subject to FTT

The main parties to the transaction, namely the purchaser and seller of shares and assimilated instruments, would be subject to the FTT, with each counterparty owing half of the overall tax charge.

Intermediaries would not be directly subject to tax, but would qualify as withholding agents.

If transactions are executed without qualifying intermediaries, the parties to the transaction would be responsible for remitting the tax.

Exemptions

Transactions with the following counterparties are exempt from FTT:

- the European Union;
- the European Central Bank;
- central banks of EU member states;
- central banks and other entities managing the official reserves of other states; and
- international entities or bodies set up by way of an international agreement executed by Italy.

The ABI has proposed an extension of the scope of the exemption to the following transactions:

- every transaction entered into by pension funds, and other complementary pension funds, governed by the Italian law;
- every transaction entered into by ''market-makers'';
- intercompany exchanges of securities, with particular attention to the business models implemented by banking groups; and
- merger and acquisition transactions executed through a sale and purchase of shares.

Withholding Agents

Banks, trustees, fiduciary companies, and all professional investment companies will qualify as withholding agents. Notaries will also qualify as intermediaries.

Under the current draft, foreign intermediaries without branch offices in Italy appear not to have withholding agent liabilities. The ABI has proposed an amendment extending withholding agent duties to foreign intermediaries, along with recognized clearinghouses. Branches would likely be deemed as withholding agents, although the language of the FTT proposal is not very clear.

Impact of FTT Omission

If no FTT is paid on transactions that are subject to tax, the related contracts would be deemed as void for all purposes.

Implementing Regulations

The Finance Ministry will issue implementing regulations for the FTT within 60 days from the entry into force of the Stability Law.

Parliamentary Review and Approval

The Stability Law and the FTT were under review by the Commissione Bilancio (budget committee) of the Chamber of Deputies, which was expected to vote on November 12. As noted, amendments may be made to the proposed FTT regime during the parliamentary review and the next Senate review. ◆

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