

ITALY – New tax regime of carried interest

The Italian Government has just introduced a new regime to regulate the taxation of carried interest and similar arrangements based on stocks or shares. The new regime should put an end to the controversy around the characterisation of benefits derived under such arrangements as income from personal services or income from investments (taxed at a more favourable rate). The new regime is contained in a decree that should be converted into law within 60 days.

Under the new regime, income and gains derived from the direct or indirect participation in companies, other entities or collective investment undertakings, established in Italy or in a jurisdiction allowing an adequate exchange of information with Italy, will be deemed to constitute investment income (taxed at 26% flat), rather than income from personal services (taxed at progressive rates up to 43% plus surcharges) when received by employees and directors of such companies, investment undertakings or other persons controlling or managing the same (e.g. employees and directors of the management company of an investment fund).

The application of the special regime is subject to the following 3 conditions:

1. the total investment commitment of all employees and directors eligible for the incentive requires an actual disbursement at least equal to 1% of total investment of the company, entity or investment undertaking;
2. income from the relevant shares, units or financial instruments accrues to the beneficiaries only after all (other) shareholders or participants have reached full repayment of the invested capital and a certain threshold return as set out in the relevant articles or regulations; in the case of disposal, the condition is referred to all other members or participants in the investment having realised upon disposal at least their invested capital and the said threshold return;
3. the relevant shares, units and financial instruments are held for no less than 5 years or, if earlier, until the date

of change of control of the relevant company or entity or change of the management company of the collective investment undertaking.

The difference between the fair market value of the shares and units received at inception and the cost paid by the relevant beneficiary will continue to be treated as income from personal services and taxed accordingly. The amount taxed as income from personal services will add up to the tax basis of the relevant instruments when computing the taxable capital gains.

The new regime will apply to proceeds and gains realised following the entry into force of the Decree (24 April 2017). Absent any indication to the contrary, this should apply also to carried interest schemes and similar arrangements put in place before that date provided that the relevant realisation of proceeds and/or gains occurs after 24 April 2017.

"This is a very welcome innovation in the Italian tax system. It will put an end to years of uncertainty and controversy, and will make Italy more attractive for top executives in the private equity industry that may consider moving to Italy", says Carlo Galli, Head of Tax at Clifford Chance Italy.

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