

In this issue:

- **Current tax treatment of foreign non-UCITS funds**
[See more ...](#)
- **Expected new tax regime**
[See more ...](#)
- **Impact for Luxembourg non-UCITS fund industry**
[See more ...](#)

Italian Tax Update 2011

New Italian tax regime for investment funds

Italy has initiated a reform regarding the taxation of Italian investment funds as well as proceeds derived by foreign EU/EEA⁽¹⁾ funds which do not qualify under the UCITS⁽²⁾ Directive 85/611 (hereafter "non-UCITS funds").

Current tax treatment of investment funds

Italian investment funds are currently subject to a substitutive tax of 12.5% calculated on any increase of the net asset value of the fund (calculation on an accrual basis). This tax is final so that Italian investors are not subject to additional taxes on income distribution or capital gains generated by these funds.

In addition, proceeds (dividends and capital gains) distributed by EU/EEA non-UCITS funds to Italian tax resident individuals follow a different tax regime as they are to be included in the total amount of the taxable income of the Italian investor and thus subject to personal progressive income tax rates up to 43%.

Expected new tax regime

On 16 February 2011, the Italian Parliament introduced a new law, aiming at modifying the taxation principles applicable to Italian investment funds and also harmonizing the taxation in Italy between UCITS and non-UCITS funds.

- **Modification of the taxation of Italian investment funds**

The new law abolishes the application of the substitutive tax applicable on the increase of the NAV and replaces it, in line with UCITS funds, by a substitutive withholding tax of 12.5% applicable on dividends and capital gains derived at the time of the disposal of their shares/units. Consequently, the taxation on an accrual basis is no longer applicable.

[Back to top](#)

⁽¹⁾ European Union/European Economic Area which includes Iceland, Liechtenstein and Norway

⁽²⁾ Undertaking for Collective Investment in Transferrable Securities

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- **New taxation principle for foreign non-UCITS funds**

Under the new Italian law, dividends and capital gains derived from EU/EEA non-UCITS funds will be subject in the hands of the Italian investors to a substitutive withholding tax of 12.5% (instead of a taxation at progressive income tax rates). The withholding tax would be levied on a cash basis.

The new regime would apply to foreign non-UCITS funds provided:

- ▶ they are established in an EU Member State or an EEA State included in the list of countries allowing the exchange of information with Italy; and
- ▶ they are subject to the supervision of the competent authorities of the State where they are established (regulated funds)

The new law harmonizes the tax treatment applicable between proceeds derived from UCITS funds (Italian or foreign) and proceeds derived from EU/EEA non-UCITS funds.

These new dispositions should enter into force as from 1 July 2011, following the final approval by the Italian Parliament which should occur within the coming weeks.

Impact for Luxembourg non-UCITS fund industry

These new rules may open borders to new investment schemes for Italian investors wishing to acquire shares/units in Luxembourg non-UCITS funds, such as Luxembourg Specialised Investment Funds. Investments in such funds would offer to Italian investors great flexibility within a regulated environment, with an attractive tax burden as proceeds derived from these Luxembourg funds would benefit from the new withholding tax rate of 12.5%.

Luxembourg, March 2011

[↶ Back to top](#)