New Double Tax Treaty between Italy and China

Tax Alert
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On 23 March 2019, the Chinese and Italian governments signed a new agreement for the avoidance of double taxation and the prevention of fiscal evasion (the 'Agreement'). The Agreement is one of the 29 commercial and trade agreements signed by the two countries during the President of China's recent visit to Italy.

The Agreement will result in a general revision of the current double tax treaty ('DTT'), signed in 1986 and in force since 1990, in order to align it with the recommendations of the OECD/G20 BEPS project. It will enter into force after its ratification by both China and Italy and after exchange of the ratification instruments.

Main amendments

The Agreement introduces new WHT rates for dividends, interest and royalties.

Income	Current DTT	Agreement
Dividends	10%	5%[a]/10%
Interest	10%	0%[b]/8%[c]/10%
Royalties	10%	5%[d]/10%

a) The WHT rate for dividends has been reduced to 5% in all cases where the beneficial owner (i) directly holds at least 25% of the share capital and (ii) meets this first condition for a minimum holding period of 365 days.

b) Exemption for interest paid to public bodies.

c) The 8% WHT applies if the interest is paid to financial institutions of the other country on loans maturing after a minimum of three years and used to fund investment projects.

d) The 10% WHT will apply only to 50% of the gross royalty (effective WHT rate of 5%) when the consideration is paid for the use of, or the right to use, industrial, commercial or scientific equipment.

Capital gains

The Agreement modifies the allocation of taxing rights: any capital gains not governed by article 13 of the DTT will be taxed only in the transferor's country of residence.

However, the source state's right to tax is confirmed when capital gains derive from the alienation of:

— immovable property;
— movable property that is part of the business property of a permanent establishment;
— shares representing at least 25% of the share capital of an entity resident in a contracting state.

KPMG's comments

The reduced WHT rates introduced by the Agreement and the likely effects of the OECD MLI (e.g. compulsory arbitration clauses in Mutual Agreement Procedures) should encourage cross-border investments and should result in greater tax efficiency, certainty and clarity for companies of both countries. At the same time, confirmation of the source state's right to tax certain capital gains, under article 13 of the DTT, could still lead to Italian tax leakage in the disposal of shares in an Italian company.

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