



Italian Tax Compliance for Swiss banks

Tax Alert

13 September 2019

Important guidance about the taxation of interest paid by Italian individuals to foreign banks can be found in two tax rulings

Tax Office Ruling no. 41 of 23 October 2018

Here, the Italian Tax Office answered a tax ruling application submitted by a Swiss bank, which had asked for clarification about the taxation of interest paid by Italian individuals under loan agreements.

The bank's query

A Swiss bank, without an Italian permanent establishment, had granted various loans to Italians (both companies and individuals), receiving interest in exchange.

The taxation of interest paid by companies was not an issue, as companies are withholding agents and no other tax obligations arose. In the case of interest paid by individuals (who are not withholding agents) the bank did not apply any kind of taxation up to 2016; instead, for fiscal year 2017 it submitted an Italian CIT return in order to tax this income.

The bank asked the Tax Office to confirm:

- its new procedure (i.e. submission of the CIT return);
- the 12.5% tax rate indicated in the DTT between Italy and Switzerland.

The Tax Office's opinion

The Tax Office described the general rule on the taxation of interest paid to foreigners by Italians - i.e. the combined provisions of articles 151 (1) and (2) and 23 (1) (b) of the Italian Income Tax Code. This rule establishes that foreigners are taxed in Italy only on Italian-source income and that capital income (such as interest) is considered to be Italian-source income if it is paid by an Italian tax resident, as in the case presented to the Tax Office.

In the case of interest paid by someone who is not a withholding agent (i.e. by an individual), the tax has to be applied in Italy through the submission of a CIT return by the foreign entity. In the fiscal years in question, the Italian CIT rate was 27.5% but this rate could be reduced under article 11 of the DTT between Italy and Switzerland, which sets a 12.5% rate if the recipient of the interest is the effective beneficial owner.

In conclusion, the Italian Tax Office accepted the bank's approach and clarified that the DTT rate of 12.5% also applies to foreign banks that receive interest payments from someone who is not a withholding agent. In this case, it is necessary for the bank to submit a CIT return.

Tax Office Ruling no. 379 of 11 September 2019

The Italian Tax Office has issued another similar tax ruling in response to an application submitted by a Swiss bank. It has substantially confirmed its previous answer of 23 October 2018. After this second reply, the position of the tax authorities is very clear.

Risks faced by foreign banks

According to the tax rulings, foreign banks which have issued loans to tax residents of Italy may have failed to file an annual CIT return in Italy to declare the income deriving from such loans.

If so, this could expose the banks to various risks:

- neglect of their obligation to submit a CIT return
- penalties and interest (on top of the tax due)
- criminal exposure (if certain thresholds are met).

Penalties, interest and criminal issues may also arise if the foreign bank has already filed an Italian CIT return, but without reporting the income from loans to Italian taxpayers.

The criminal implications are particularly far-reaching as they could affect the directors and shareholders, and even third parties, and have a direct impact on the bank's assets.

The tax rulings only describe the situation where an Italian taxpayer is an individual who is not paying interest to the bank through an Italian intermediary.

The Italian Tax Office did not explain what happens if such loans are issued to shell companies (especially those located in tax havens) and the actual beneficial owner of the loan is the Italian individual.

KPMG assistance

KPMG could assist your bank in the following way.

- KPMG Italy and KPMG Switzerland could apply their wide experience in this area by working shoulder to shoulder to audit your bank and see whether it faces any tax or criminal risks.
- If any oversights emerge, we could:
 - calculate the taxes, penalties and interest;
 - help you to regularize your position with the Italian Tax Office;
 - prepare and file your CIT returns;
 - assist you in handling any criminal exposure.

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