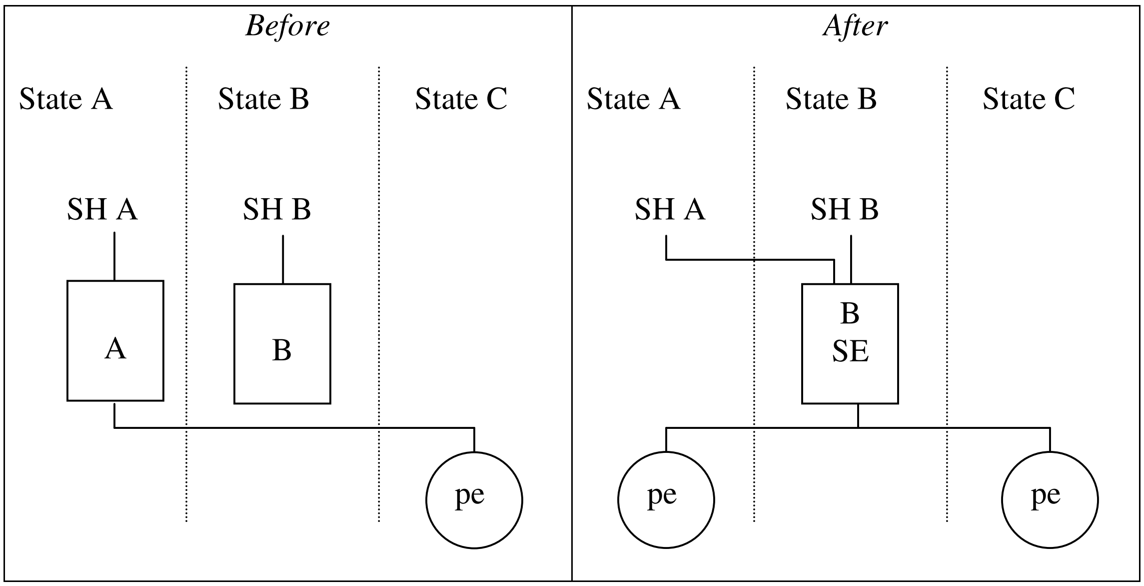
Annex 9 - Italy

ITALY

CASE 1

Merger by acquisition

(Art. 2 par. 1 jo. Art 17 par. 2(a) Reg. 2157/2001)



Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A and B are existing companies
- A and B are public limited-liability companies (see Annex I to Reg. 2157/2001)
- State A, State B, and State C are EU Member States
- A:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A
  - has a permanent establishment in Member State C
- B:
  - formed under law of Member State B
  - registered office in Member State B
  - head office in Member State B
- B SE:
  - registered office in Member State B
  - head office in Member State B
  - will be covered by the EC Merger Directive

Transactions

- A:
  - transfers all assets and liabilities to B
  - in exchange for shares in B (and cash payment if any, not exceeding 10% of nominal value of shares to be issued) issued to shareholder(s) of A
  - will be wound up without going into liquidation

- B / B SE:
  - as the acquiring company, B will take the form of an SE when the merger takes place (Art. 17 Reg. 2157/2001: "In the case of a merger by acquisition, the acquiring company shall take the form of an SE when the merger takes place". Consequently, there are in fact two transactions: 1) the merger and 2) a transformation of a public limited-liability company into an SE. With regard to the transformation, see also Case 9.)
  - will be regarded as public limited-liability company governed by law of Member State B

Questions

1) Assume Member State A is your country

   <u>Tax effects for A in Member State A</u>

   a) Will the merger give rise to any taxation of capital gains (= real value of assets & liabilities transferred minus their value for tax purposes), or is there roll-over relief?

      According to Art. 2 of the Decree No. 544 of 1992, if the assets and liabilities of an Italian company are transferred to a receiving company in another Member State, the capital gain may be rolled over to the receiving company. See, however, answer to e) below as regard a permanent establishment.
      The business transferred must, however, constitute a permanent establishment in Italy of the receiving company resident in another Member State. The concept of permanent establishment is not defined under Italian law. Probably the relevant treaty definition will apply.
      The assets and liabilities transferred, which are not included in the Italian permanent establishment of the receiving company, are deemed to have been transferred at market value for the purposes of taxing the capital gain.

   b) May provisions and reserves, which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State A, be taken over with the same roll-over relief by the permanent establishment of B SE in Member State A?

Such provisions and reserves can be taken over by the permanent establishment in Italy, provided that they are reinstated in the balance sheet of the Italian post-merger permanent establishment.

According to Art. 3 of the Decree No. 544 of 1992, tax-deferred reserves entered in the last balance sheet of the transferring company not reinstated in the balance sheet of the Italian post-merger permanent establishment of the receiving company are subject to tax in Italy in the hands of the non-resident company.

c) Will B SE's permanent establishment in Member State A be allowed to take over the losses of A that have not been exhausted for tax purposes? If B SE would be a company resident in Member State A, would it then be allowed to take over these losses?

The Decree No. 544 of 1992 expressly points to the rules applicable to domestic companies. According to Art. 4 of the Decree No. 544 of 1992, losses generated by the Italian resident transferring company can be used by the foreign receiving company under the limitations provided for in Art. 123, paragraph 5 of the CITA (Consolidated Income Tax Act) in proportion to the difference between the assets and liabilities effectively connected with the PE in Italy and up to such difference.

d) Will Member State A renounce any right to tax the permanent establishment in Member State C?

See e) below.

e) Or will Member State A tax profits or capital gains with respect to the permanent establishment as a result of the merger? If so, will Member State A give relief for any (notional) tax charged on these profits or capital gains by Member State C?

According to Art. 2 paragraph 3 of the Decree No. 544 of 1992, the PE will be considered as if it had been disposed at market value but a (notional) tax credit will be granted. The tax credit is equal to the tax that the State where the PE is located would have charged in the absence of the Merger Directive.

f) Will Member State A reinstate in the taxable profits of A such losses of the permanent establishment as have been set off against the taxable profits of A in Member State A and which have not been recovered at the time of the merger?

No, Italy applies foreign tax credit to relieve international double taxation. See e) above.

Tax effects for SH A in Member State A

g) Will the issue of shares by B SE to SH A, resident in Member State A, in exchange for shares in A give rise to any taxation of the income, profits or capital gains of that shareholder?

According to Art. 2 paragraph 5 of the Decree No. 544 of 1992, the allotment of shares representing the capital of the receiving company to a shareholder of the transferring company in exchange for shares representing the capital of the latter company, does not give rise to any taxation in the hands of that shareholder. The fiscal value of the cancelled shares will constitute the tax basis of the shares received in exchange. Any cash payment received by the shareholder is taxable. [This may constitute a problem since the tax value of the shares is not accordingly increased (see Maisto, The implementation …, p.486)]

h) Will the issue of shares by B SE to a shareholder of A, not resident in Member State A, in exchange for shares in A give rise to any taxation of the income, profits or capital gains of that shareholder?

Under Italian domestic law, gains realized on the alienation of shares in the capital of an Italian resident company are in principle taxable in Italy. However, according to Art. 2 paragraph 5 of the Decree No. 544 of 1992, if at least one of the participants is resident in Italy or the participation exchanged is effectively connected with a permanent establishment in Italy of a company listed in the Annex to the Directive, roll-over relief is available.
Consequently, after the merger, Italy may very likely lose its tax claim since the non-resident shareholder of the non-resident receiving company may be taxed in Italy only if the certificates of the shares are physically located in Italy.
The relevance of the problem is, however, limited since specific exemption are already established in Italian domestic law for non-resident shareholders alienating non-substantial participations in quoted companies and in non-quoted companies if the shareholder is resident in a Country included in the list ("white list") issued by the ministry of Finance. Moreover, in most of its tax treaties, Italy has given up its right to tax such gains. Exceptions to the general rule of taxation in the residence state of the alienator are contained in the treaties with France (capital gains on shares in companies whose assets consist of immovable property), United Kingdom (capital gains on shares in Italian companies accruing to Italian national who moved to the United Kingdom less than five years prior to the transfer if the gain is not subject to tax in the United Kingdom) and the Netherlands (capital gains on shares in Italian companies accruing to Italian national who moved to the United Kingdom less than five years prior to the transfer).

i) Will the answers to the questions 1g) and 1h) differ if SH A is:
   i) A corporate shareholder?
   ii) An individual shareholder not owning a substantial interest?
   iii) An individual shareholder owning a substantial interest?
   iv) An individual entrepreneur?

   No, it will not. Note however that a different tax treatment may be applied as regard the cash payment, if any.

2) Assume Member State B is your country

   <u>Tax effects for B and B SE in Member State B</u>

   a) According to Art. 17 par. 2 Reg. 2157/2001, the acquiring company shall take the form of an SE when the merger takes place. According to Art. 37 par. 2 Reg. 2157/2001 the conversion of a public limited-liability company into an SE shall not result in the winding up of the company or in the creation of a new legal person. However, the Regulation itself does not give guidance with regard to taxation. Will the fact that B takes the form of an SE have corporate income tax consequences in Member State B?

      No, according to Art. 122 of CITA it will not have any consequences.

   b) What is the value for tax purposes that B SE has to attribute to the assets and liabilities, which are transferred to B SE as part of the merger and that form a permanent establishment in Member States A and C?

      Art. 2 paragraph 1 of the Decree No. 544 of 1992 applies to this case. Accordingly, the value that for tax purposes the resident receiving company has to attribute to the assets and liabilities of the transferring company is the last tax value the assets and liabilities had in the hands of the transferring company. If the acquiring company increases the book value because of the imputation of the merger deficit, a statement has to be attached to the tax return showing the difference between the book value and the tax value of each asset.
      Note that, regarding the PE in a third EU State (i.e. State C) of the transferring company (i.e. company A), if the State of the transferring company taxes the capital gain arising from the alienation of the foreign PE, then the tax value of the PE will be equal to its market value.

   <u>Tax effects for SH B in Member State B</u>

   c) Will the fact that B will take the form of an SE result in tax consequences for SH B?

      It seems that Art. 2 paragraph 5 of the Decree No. 544 of 1992 applies to this case. Accordingly, the fiscal value of the cancelled shares will constitute the tax *basis of the shares received in exchange. Any cash payment received by the shareholder is taxable.*

d) Will the answer to question 2c) above differ if SH B is:
   i) A corporate shareholder?
   ii) An individual shareholder not owning a substantial interest?
   iii) An individual shareholder owning a substantial interest?
   iv) An individual entrepreneur?

   No, it will not be different. Note however that a different tax treatment may be applied as regard the cash payment, if any.

3) Assume Member State C is your country

<u>Tax effects for A and B SE in Member State C with respect to its permanent establishment in Member State C</u>

a) Will the merger give rise to any taxation in (the hands of) A of capital gains (= real value of assets & liabilities transferred minus their value for tax purposes) or is there roll-over relief?

   The transfer does not result in any taxation in Italy. According to Art. 2 paragraph 2 of the Decree No. 544 of 1992, the assets and liabilities of the PE maintain their pre-merger value for Italian tax purposes.

b) May provisions and reserves, which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State C, be taken over with the same roll-over relief by the permanent establishment of B SE in Member State C?

   It is doubtful. Art. 3 of the Decree No. 544 of 1992 only refers to the tax-deferred reserves and provisions included in the last balance sheet of the resident transferring company. Accordingly, it could be concluded that the non-reinstatement of tax-deferred reserves and provisions in the balance sheet of the non-resident receiving company does not lead to any taxation in Italy, but this conclusion seems not to be in line with the spirit and purpose of the Decree No. 544 of 1992.

c) Will B SE's permanent establishment in Member State C be allowed to take over the losses of A's permanent establishment that have not been exhausted for tax purposes?

   It is doubtful. Art. 4 of the Decree No. 544 of 1992 allows the carry-over of losses to the non-resident receiving company only for the operations referred to in Art. 1 paragraphs a) and b) of the Decree No. 544 of 1992. These paragraphs relate *however only to the merger or division involving a resident company and another EU Member State resident company. From a literal interpretation of the rule, it seems that such carry-over would not apply to the case under discussion.*

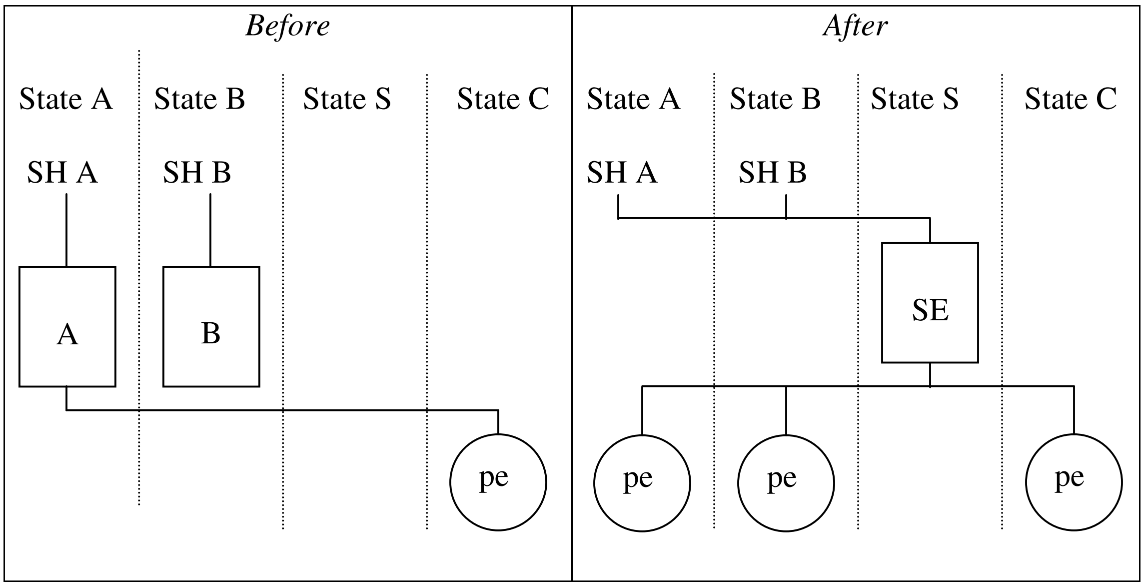
d) If B SE would be a company resident in Member State C, would it then be allowed to take over these losses? See Merger Directive Art. 6.

The same problem discussed above arises. Distinguished scholars believe however that in such case, the resident receiving company should be allowed to carry-over the losses of the pre-merger Italian PE (as if the PE were a resident company) under the limitations provided for in Art. 123, paragraph 5 of the CITA (Consolidated Income Tax Act) in proportion to the difference between the assets and liabilities effectively connected with the PE in Italy and up to such difference but the wording of Art. 4 of the Decree No. 544 of 1992 does not seem to allow this conclusion.

CASE 2

Merger by formation of a new company

(Art. 2 par. 1 jo Art 17. par 2(b) Reg. 2157/2001)



Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A and B are existing companies
- A has a permanent establishment in Member State C
- SE is a new company
- A and B are public limited-liability companies (see Annex I to Reg. 2157/2001)
- State A, State B, State C, and State S are EU Member States
- A:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A
- B:
  - formed under law of Member State B
  - registered office in Member State B
  - head office in Member State B
- SE:
  - formed under law of Member State S
  - registered office in Member State S
  - head office in Member State S
  - will be covered by the EC Merger Directive

Transactions

- A:
  - transfers all assets and liabilities to SE
  - in exchange for shares of SE (and cash payment if any, not exceeding 10% of nominal value of shares to be issued) issued to shareholder(s) of A
  - will be wound up without going into liquidation
- B:
  - transfers all assets and liabilities to SE
  - in exchange for shares of SE (and cash payment if any, not exceeding 10% of nominal value of shares to be issued) issued to shareholder(s) of B
  - will be wound up without going into liquidation
- SE:
  - will be a newly formed SE
  - will be regarded as public limited-liability company governed by the law of Member State S

Questions

1) Assume Member State A is your country

   <u>Tax effects for A in Member State A</u>

   a) Will the merger give rise to any taxation of capital gains (= real value of assets & liabilities transferred minus their value for tax purposes), or is there roll-over relief?

      According to Art. 2 of the Decree No. 544 of 1992, if the assets and liabilities of an Italian company are transferred to a receiving company in another Member State, the capital gain may be rolled over to the receiving company. See, however, answer to e) below as regard a permanent establishment.
      The business transferred must, however, constitute a permanent establishment in Italy of the receiving company resident in another Member State. The concept of permanent establishment is not defined under Italian law. Probably the relevant treaty definition will apply.
      The assets and liabilities transferred, which are not included in the Italian permanent establishment of the receiving company, are deemed to have been transferred at market value for the purposes of taxing the capital gain.

   b) May provisions and reserves, which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State A, be taken over with the same roll-over relief by the permanent establishment of SE in Member State A?

Such provisions and reserves can be taken over by the permanent establishment in Italy, provided that they are reinstated in the balance sheet of the Italian post-merger permanent establishment.

According to Art. 3 of the Decree No. 544 of 1992, tax-deferred reserves entered in the last balance sheet of the transferring company not reinstated in the balance sheet of the Italian post-merger permanent establishment of the receiving company are subject to tax in Italy in the hands of the non-resident company.

c) Will SE's permanent establishment in Member State A be allowed to take over the losses of A that have not been exhausted for tax purposes? If SE would be a company resident in Member State A, would it then be allowed to take over these losses?

The Decree No. 544 of 1992 expressly points to the rules applicable to domestic companies. According to Art. 4 of the Decree, losses generated by the Italian resident transferring company can be used by the foreign receiving company under the limitations provided for in Art. 123, paragraph 5 of the CITA (Consolidated Income Tax Act) in proportion to the difference between the assets and liabilities effectively connected with the PE in Italy and up to such difference.

d) Will Member State A renounce any right to tax the permanent establishment in Member State C?

See f) below.

e) Will Member State A reinstate in the taxable profits of A such losses of the permanent establishment as have been set off against the taxable profits of A in Member State A and which have not been recovered at the time of the merger?

No, Italy applies foreign tax credit to relieve international double taxation. See f) below.

f) Or will Member State A tax profits or capital gains of the permanent establishment resulting from the merger? If so, will it give relief for any (notional) tax charged on these profits or capital gains by Member State C?

According to Art. 2 paragraph 3 of the Decree No. 544 of 1992, the PE will be considered as if it had been disposed at market value but a (notional) tax credit will be granted. The tax credit is equal to the tax that the State where the PE is located would have charged in the absence of the Merger Directive.

Tax effects for SH A in Member State A

g) Will the issue of shares by SE to SH A, resident in Member State A, in exchange for the shares in A give rise to any taxation of the income, profits or capital gains of that shareholder or is there roll-over relief?

According to Art. 2 paragraph 5 of the Decree No. 544 of 1992, the allotment of shares representing the capital of the receiving company to a shareholder of the transferring company in exchange for shares representing the capital of the latter company, does not give rise to any taxation in the hands of that shareholder. The fiscal value of the cancelled shares will constitute the tax basis of the shares received in exchange. Any cash payment received by the shareholder is taxable. [This may constitute a problem since the tax value of the shares is not accordingly increased (see Maisto, The implementation …, p.486)]

h) Will the issue of shares by SE to a shareholder of A, not resident in Member State A, in exchange for the shares in A give rise to any taxation of the income, profits or capital gains of that shareholder or is there roll-over relief?

Under Italian domestic law, gains realized on the alienation of shares in the capital of an Italian resident company are in principle taxable in Italy. However, according to Art. 2 paragraph 5 of the Decree No. 544 of 1992, roll-over relief is available. Consequently, after the merger, Italy may very likely lose its tax claim since the non-resident shareholder of the non-resident receiving company may be taxed in Italy only if the certificates of the shares are physically located in Italy. The relevance of the problem is, however, limited since specific exemption are already established in Italian domestic law for non-resident shareholders alienating non-substantial participations in quoted companies and in non-quoted companies if the shareholder is resident in a Country included in the list ("white list") issued by the ministry of Finance. Moreover, in most of its tax treaties, Italy has given up its right to tax such gains. Exceptions to the general rule of taxation in the residence state of the alienator are contained in the treaties with France (capital gains on shares in companies whose assets consist of immovable property), United Kingdom (capital gains on shares in Italian companies accruing to Italian national who moved to the United Kingdom less than five years prior to the transfer if the gain is not subject to tax in the United Kingdom) and the Netherlands (capital gains on shares in Italian companies accruing to Italian national who moved to the United Kingdom less than five years prior to the transfer).

i) Will the answers to the questions 1g) and 1h) differ if SH A is:
   i) A corporate shareholder?
   ii) An individual shareholder not owning a substantial interest?
   iii) An individual shareholder owning a substantial interest?
   iv) An individual entrepreneur?

   No, it will not. Note however that a different tax treatment may be applied as regard the cash payment, if any.

2) Assume Member State S is your country

   <u>Tax effects for SE in Member State S</u>

   a) What is the value for tax purposes that SE has to attribute to the assets and liabilities, which are transferred to SE as part of the merger and that form a permanent establishment in Member States A, B and C?

      Art. 2 paragraph 1 of the Decree No. 544 of 1992 applies to this case. Accordingly, the value that for tax purposes the resident receiving company has to attribute to the assets and liabilities of the transferring company is the last tax value the assets and liabilities had in the hands of the transferring company. If the acquiring company increases the book value because of the imputation of the merger deficit, a statement has to be attached to the tax return showing the difference between the book value and the tax value of each asset.
      Note that, regarding the PE in a third EU State (i.e. State C) of the transferring company (i.e. company A), if the State of the transferring company taxes the capital gain arising from the alienation of the foreign PE, then the tax value of the PE will be equal to its market value.

   <u>Tax effects for shareholder(s) of SE in Member State S</u>

   b) Is there any provision in the legislation of Member State S that affects the shareholder of SE whether resident in Member State S or not? For example, are there provisions with regard to the valuation of the shares received in SE?

      The Decree No. 544 of 1992 applies to this case and, according to Art. 2 paragraph 5, the fiscal value of the cancelled shares will constitute the tax basis of the shares received in exchange. Any cash payment received by the shareholder is taxable.

3) Assume Member State C is your country

<u>Tax effects for A and SE in Member State C in respect of its permanent establishment in Member State C</u>

a) Will the merger give rise to any taxation of capital gains (= real value of assets & liabilities transferred minus their value for tax purposes) or is there roll-over relief?

The transfer does not result in any taxation in Italy. According to Art. 2 paragraph 2 of the Decree No. 544 of 1992, the assets and liabilities of the PE maintain their pre-merger value for Italian tax purposes.

b) May provisions and reserves, which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State C, be taken over with the same roll-over relief by the permanent establishment of SE in Member State C?

It is doubtful. Art. 3 of the Decree No. 544 of 1992 only refers to the tax-deferred reserves and provisions included in the last balance sheet of the resident transferring company. Accordingly, it could be concluded that the non-reinstatement of tax-deferred reserves and provisions in the balance sheet of the non-resident receiving company does not lead to any taxation in Italy, but this conclusion seems not to be in line with the spirit and purpose of the Decree.

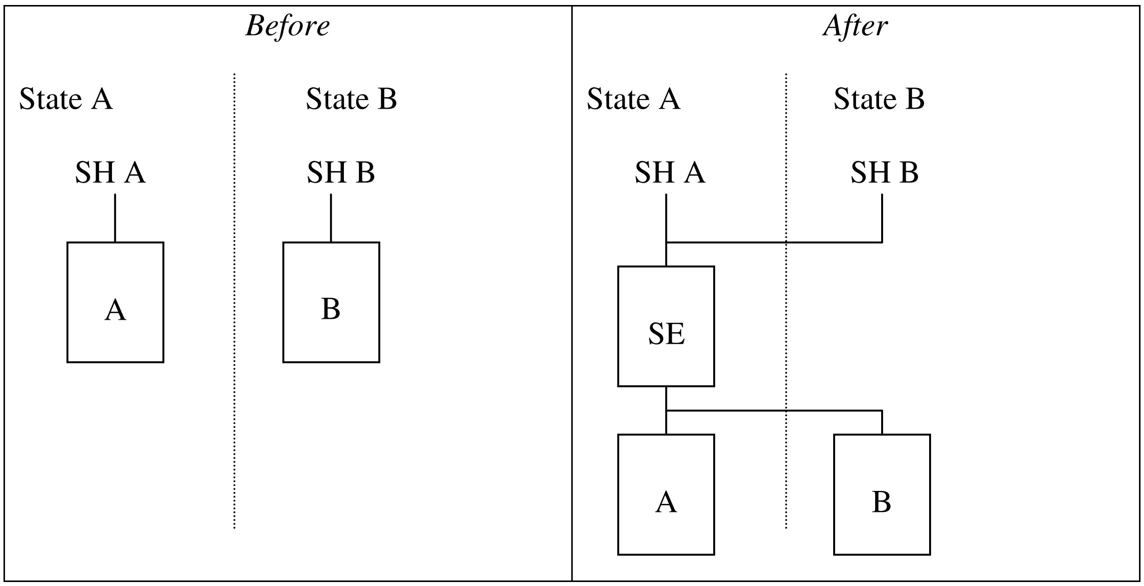
c) Will SE's permanent establishment in Member State C be allowed to take over the losses of A's permanent establishment that have not been exhausted for tax purposes? If SE would be a company resident in Member State C, would it then be allowed to take over these losses?

It is doubtful. Art. 4 of the Decree No. 544 of 1992 allows the carry-over of losses to the non-resident receiving company only for the operations referred to in Art. 1 paragraphs a) and b) of the Decree No. 544 of 1992. These paragraphs relate however only to the merger or division involving a resident company and another EU Member State resident company. From a literal interpretation of the rule, it seems accordingly that such carry-over would not apply to the case under discussion. The same problem arises if SE would be a company resident in State C. Distinguished scholars believe, however, that in such case, the resident receiving company should be allowed to carry-over the losses of the pre-merger Italian PE (as if the PE were a resident company) under the limitations provided for in Art. 123, paragraph 5 of the CITA (Consolidated Income Tax Act) in proportion to the difference between the assets and liabilities effectively connected with the PE in Italy and up to such difference but the wording of Art. 4 of the Decree No. 544 of 1992 does not seem to allow such conclusion.

CASE 3

Formation of a Holding – SE – 1

(Art. 2 par. 2(a) jo. Art. 32, Art. 33 and Art. 34 Reg. 2157/2001)



Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A and B are existing companies
- SE is a new company
- A and B are public or private limited-liability companies (see Annex II Reg. 2157/2001)
- State A and State B are EU Member States
- A:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A
- B:
  - formed under law of Member State B
  - registered office in Member State B
  - head office in Member State B
- SE:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A
  - will be covered by the EC Merger Directive

Transactions

- SE:
    - will be regarded as public limited-liability company governed by the law of Member State A
    - acquires holding in A and B
    - such that it obtains more than 50% of the permanent voting rights in A and B
    - in exchange for shares in SE
    - issued to the shareholders of A and B

Questions

1) Assume Member State A is your country

<u>Tax effects for SE in Member State A</u>

a) Are there any provisions for the valuation for tax purposes of the shares in A and B acquired by SE? Do the shares have to be valued at the book value of the exchanging shareholder or at a higher value?

See answer to question b) below.

b) Are there any provisions for the valuation for tax purposes of the shares issued to SH A and SH B? Do the shares have to be valued at the book value of the shares exchanged by the shareholder or at a higher value?

The exchange of shares between SH A and SE does not qualify under the Decree No. 544 of 1992 implementing the merger directive since the acquiring and the acquired company reside in the same Member State. As a consequence, the rule on the domestic exchange of shares will apply. On the other hand, the exchange of shares between SH B and SE does qualify under the Decree No. 544 of 1992 implementing the merger directive since the acquiring and the acquired company reside in two different Member States.

Regarding the exchange of shares between SH A and SE
Decree No. 358 of 1997 provides for two different regimes depending on whether the shares allotted to the shareholders of the acquired company are existing shares or new issued shares.

Allotment of existing shares ("permuta di azioni")
The conditions to apply such regime are that:
- the acquiring company is a public limited liability company (i.e., not an SRL) resident in Italy;
- the acquired company is a company subject to CIT (i.e., also an SRL) resident in Italy

According to the Ministry of Finance (Circular Letter 320/E of 1997), the shareholders of the acquired company need not to be entrepreneurs.
According to Art. 5 paragraph 1 of the Decree No. 358, the exchange of shares is tax neutral if the book value of the transferred shares is carried over the shares received in exchange. Any cash or in kind payment ("conguaglio") is taxable in the hands of the recipient and, different from the merger directive, no 10% limit applies.
If the value entered in the accounts of the acquiring company is higher than that the shares given in exchange had before the transaction, then there will be ordinary taxation of the capital gain.
If, however, the acquiring company has held the exchanged shares for more than three years and has registered them as fixed asset, then it may opt for the payment of a substitute tax equal to 19% of the capital gain. The substitute tax is not deductible for income tax purposes.
Note that, both in case of ordinary taxation and in case of application of the substitute tax, the capital gain will be computed on the normal value of shares and not on the book value given to them in the accounts of the acquiring company.

Allotment of new issued shares
The conditions to apply such regime are that:
- the acquired and the acquiring company are company resident in Italy and subject to CIT;
- the shareholders of the acquired company is an entrepreneur.
According to Art. 5 paragraph 2 of the Decree No. 358, in order to determine the gain realized by the acquiring company, the value of the shares in the acquired company is equal to the registered increase in the net equity of that company as a consequence of the transfer.

Regarding the exchange of shares between SH B and SE
The Decree No. 544 of 1992, implementing the merger directive applies to this case. Note that, different from the merger directive, the Decree requires that at least one of the participants be resident in Italy or that the participation exchanged be effectively connected with a permanent establishment in Italy of a company listed in the Annex to the Directive.
According to distinguished authors, Art. 2 paragraph 5 does not require that the tax basis of the acquired shares for the acquiring company be the same as that recognized for the participants and consequently the value for tax purposes for the acquiring company is the real value of the shares acquired.

It may be argued, however, that Art. 2 paragraph 5 applies also to the receiving company and that the exchange of shares is tax neutral and the tax value of the received shares is equal to the tax value of the exchanged shares before the transaction.

<u>Tax effects for SH A in Member State A</u>

c) Will the issue of shares by SE to SH A in exchange for shares in A give rise to any taxation of the income, profits or capital gains of SH A or is there roll-over relief?
d) Will the answers to the question 1c) differ if SH A is:
   i) A corporate shareholder?
   ii) An individual shareholder not owning a substantial interest?
   iii) An individual shareholder owning a substantial interest?
   iv) An individual entrepreneur?

Regarding the exchange of shares between SH A and SE
Decree No. 358 of 1997 provides for two different regimes in case the shares allotted to the shareholders of the acquired company are already existing shares or new issued shares.

Allotment of existing shares ("permuta di azioni")
The conditions to apply such regime are that:
- the acquiring company is public limited liability company (i.e., not an SRL) resident in Italy;
- the acquired company is a company subject to CIT (i.e., also an SRL) resident in Italy
According to the Ministry of Finance (Circular Letter 320/E of 1997), the shareholders of the acquired company need not to be entrepreneurs.
According to Art. 5 paragraph 1 of the Decree No. 358, the exchange of shares is tax neutral if the book value of the transferred shares is carried over the shares received in exchange. Any cash or in kind payment ("conguaglio") is taxable in the hands of the recipient and no 10% limit, as under the directive, applies.
If the value entered in the accounts of the acquiring company is lower than that the shares given in exchange had before the transaction, then there will be ordinary taxation of the capital gain.
If, however, the shareholder is an entrepreneur who has held the exchanged shares for more than three years and has registered them as fixed asset, then it may opt for the payment of a substitute tax equal to 19% of the capital gain. The substitute tax is not deductible for income tax purposes.
Note that, both in case of ordinary taxation and in case of application of substitute tax, the capital gain will be computed on the normal value of shares and not on the book value given to them in the accounts of the acquiring company.

Allotment of new issued shares
The conditions to apply such regime are that:
- the acquired and the acquiring company are company resident in Italy and subject to CIT;
- the shareholders of the acquired company is an entrepreneur.

According to Art. 5 paragraph 2 of the Decree No. 358, if the increase in the net equity registered by the acquiring company is higher than the tax value the shares of the acquired company had before the transaction in the hands of the shareholders, then there will be ordinary taxation of the capital gain so determined. If, however, the shareholder has held the exchanged shares for more than three years and has registered them as fixed asset, then it may opt for the payment of a substitute tax equal to 19% of the capital gain. The substitute tax is not deductible for income tax purposes.

2) Assume Member State B is your country

<u>Tax effects for SH B in Member State B</u>

a) Will the issue of shares by SE to SH B in exchange for shares in B give rise to any taxation of the income, profits or capital gains of SH B or is there roll-over relief?

   The Decree No. 544 of 1992, implementing the merger directive, applies to this case.
   Note that, different from the merger directive, the Decree requires that at least one of the participants be resident in Italy or that the participation exchanged be effectively connected with a permanent establishment in Italy of a company listed in the Annex to the Directive.
   According to Art. 2 paragraph 5, the exchange of shares is tax neutral and the tax value of the received shares is equal to the tax value of the exchanged shares before the transaction. Cash payments are taxable in the hands of the recipient.

b) Will the answers to the question 1a) differ if SH B is:
   i) A corporate shareholder?
   ii) An individual shareholder not owning a substantial interest?
   iii) An individual shareholder owning a substantial interest?
   iv) An individual entrepreneur?

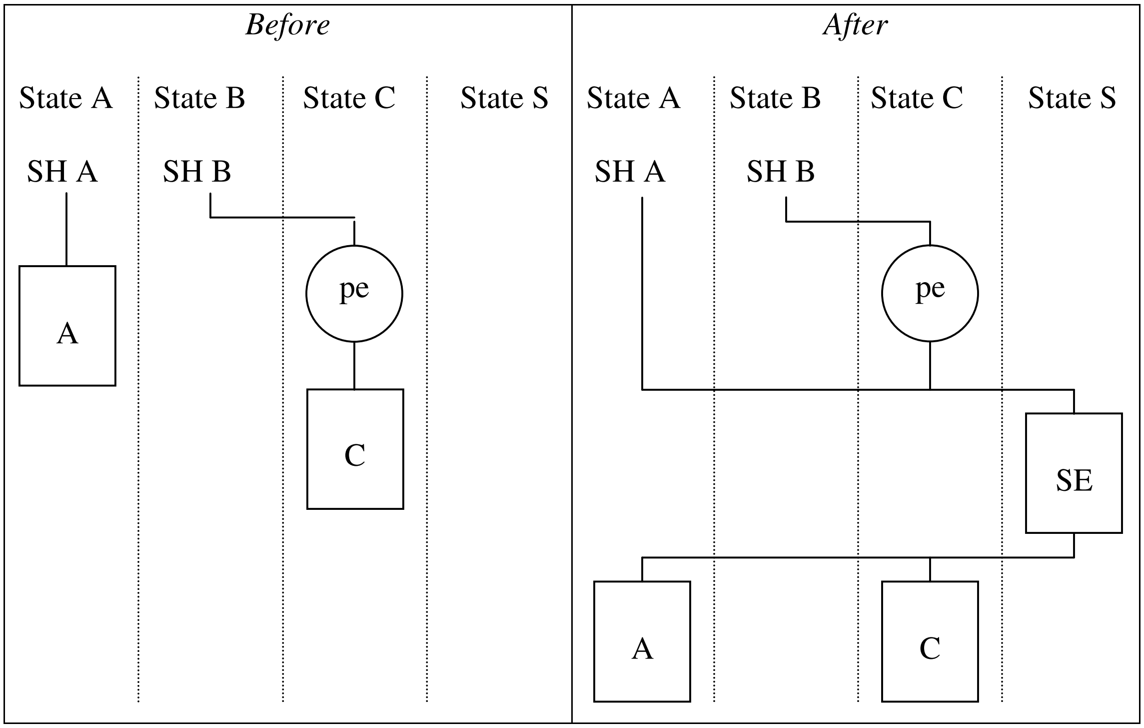
   No, it will not make any difference. Note however that a different tax treatment may be applied as regard the cash payment, if any.

   *Note***
   [The Bill containing the guidelines for a comprehensive tax reform currently before the Parliament provides for the abolition of the substitute tax provided for in the Decree No. 358 of 1997 and for the maintenance of the neutrality regime as provided for by the mentioned Decree and the Decree No. 544 of 1992]

CASE 4

Formation of a Holding – SE

(Art. 2 par. 2(a) and (b) jo. Art. 32, Art. 33, and Art. 34 Reg. 2157/2001)



Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A and C are existing companies
- The shares in C are attributable to pe in State C
- SE is a new company
- A and C are public or private limited-liability companies (see Annex II)
- State A, State B, State C and State S are EU Member States
- A:
    - formed under law of Member State A
    - registered office in Member State A
    - head office in Member State A
- C:
    - formed under law of Member State C
    - registered office in Member State C
    - head office in Member State C
- SE:
    - formed under law of Member State S

- registered office in Member State S
- head office in Member State S
- will be covered by the EC Merger Directive

Transactions

- SE:
    - will be regarded as public limited-liability company governed by the law of Member State S
    - acquires holding in A and C
    - such that it obtains more than 50% of the permanent voting rights in A and C
    - in exchange for shares in SE
    - issued to the shareholders of A and C

Questions

1) Assume Member State A is your country

<u>Tax effects for SH A in Member State A</u>

a) Will the issue of shares by SE to SH A in exchange for shares in A give rise to any taxation of the income, profits or capital gains of SH A or is there roll-over relief?

   According to Art. 2 paragraph 5 of the Decree No. 544 of 1992, the allotment of shares representing the capital of acquiring company to a shareholder of the acquired company in exchange for shares representing the capital of the latter company, does not give rise to any taxation in the hands of that shareholder. The fiscal value of the transferred shares will constitute the tax basis of the shares received in exchange. Any cash payment received by the shareholder is taxable.

b) Will the answer to the above question be different in the case of:
   i) SH A being an individual shareholder not owning a substantial interest?
   ii) SH A being an individual shareholder owning a substantial interest?
   iii) SH A being an individual entrepreneur?
   iv) SH A being a corporate shareholder?

   No, it will not.

2) Assume Member State B is your country

<u>Tax effects for SH B in Member State B</u>

a) Will the issue of shares by SE to SH B in exchange for shares in C give rise to any taxation of the income, profits or capital gains of SH B or is there roll-over relief?

According to Art. 2 paragraph 5 of the Decree No. 544 of 1992, the allotment of shares representing the capital of acquiring company to a shareholder of the acquired company in exchange for shares representing the capital of the latter company, does not give rise to any taxation in the hands of that shareholder. The fiscal value of the transferred shares will constitute the tax basis of the shares received in exchange. Any cash payment received by the shareholder is taxable.

b) Will the answer to the above question be different in the case of:
   i) SH B being an individual entrepreneur?
   ii) SH B being a corporate shareholder?

No, it will not.

3) Assume Member State C is your country

<u>Tax effects for SH B in Member State C</u>

a) Will the issue of shares by SE to SH B in exchange for shares in C give rise to any taxation of the income, profits or capital gains of SH B or is there roll-over relief?

See b) below.

b) Will the answer to the above question be different in the case of:
   i) SH B being an individual entrepreneur?
   ii) SH B being a corporate shareholder?

In case of exchange of shares, the Decree No. 544 of 1992 provides for roll-over relief only if there is at least one Italian resident participant or the shares are held through an Italian permanent establishment of a company listed in the Annex to the Directive.
Accordingly, if SH B is a company listed in the annex of the Directive, then it will carry the value of the shares in company C over the value of the shares in SE. On the other hand, if SH B is not a company listed in the annex, then the capital gain will be taxable in Italy. In this respect, Italy's right to tax the capital gain in the hands of the non-resident shareholder is not restricted by the treaty concluded

with the country of residence of the shareholder because the holding is effectively connected with a permanent establishment in Italy.
It seems that the requirement set in the Decree No. 544 of 1992 is against the Directive, which does not contain any specific provision concerning the qualification of the shareholder.

4) Assume Member State S is your country

<u>Tax effects for SE in Member State S</u>

a) Are there any provisions for the valuation for tax purposes in Member State S of the shares of A and C acquired by SE? Do the shares have to be valued at the book value of the exchanging shareholder or at a higher value?

See b) below.

b) Are there any provisions for the valuation for tax purposes in Member State S of the shares issued to SH A and SH B? Do the shares have to be valued at the book value of the shares exchanged by the shareholder or at a higher value?

The Decree No. 544 of 1992 requires that at least one of the participants be resident in Italy or that the participation exchanged be effectively connected with a permanent establishment in Italy of a company listed in the Annex to the Directive. It is doubtful whether the term participants ("partecipanti") has to be interpreted as referring only to the shareholders of the acquired company or also to the acquiring company.

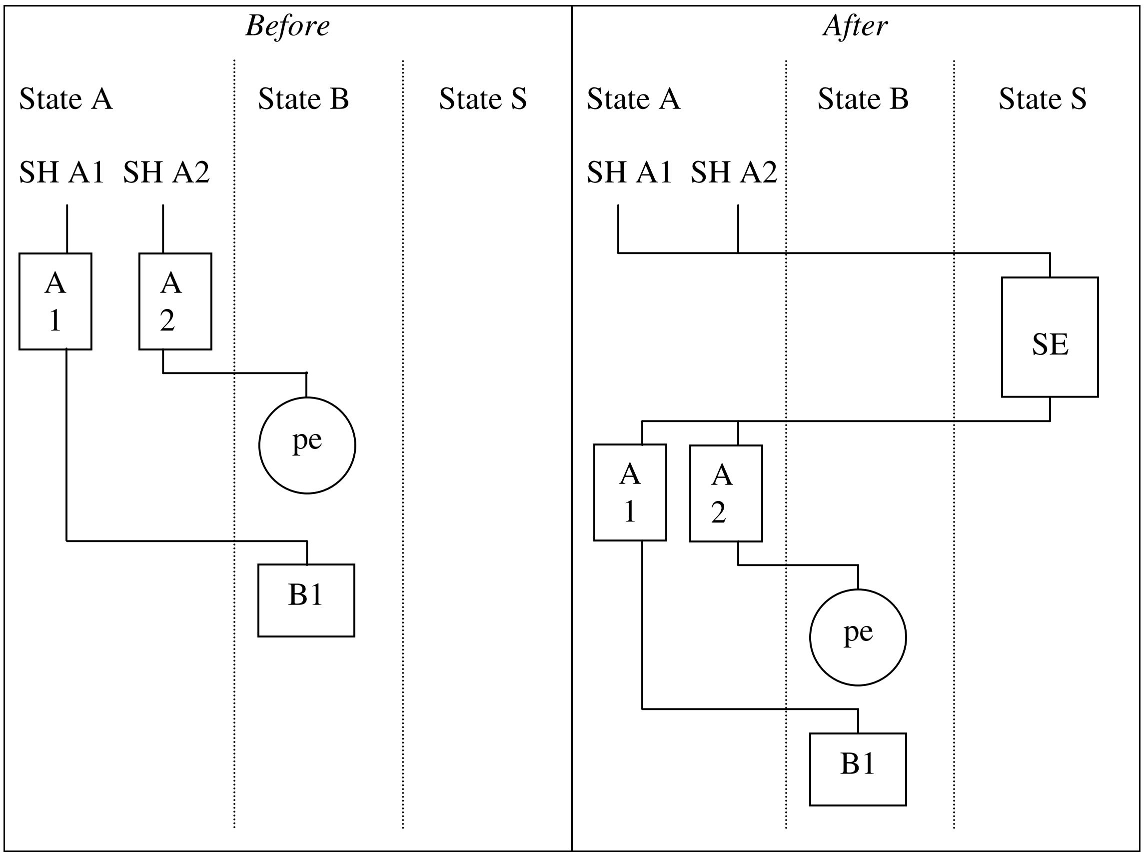
In the former case, the Decree is not applicable and accordingly the acquiring company may evaluate the received shares at their market value.
In the latter case, the Decree is applicable. However, even though the Decree in general applies, according to distinguished authors, Art. 2 paragraph 5 does not require that the tax basis of the acquired shares for the acquiring company be the same as that recognized for the participants and consequently the value for tax purposes for the acquiring company is the real value of the shares acquired.

It may be argued, however, that Art. 2 paragraph 5 applies also to the receiving company and that the exchange of shares is tax neutral and the tax value of the received shares is equal to the tax value of the exchanged shares before the transaction.

CASE 5

Formation of a Holding – SE

(Art. 2 par. 2(b) jo. Art. 32, Art. 33, and Art. 34 Reg. 2157/2001)



Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A1, A2, and B1are existing companies
- pe is an existing permanent establishment of A2 in Member State B
- SE is a new company
- A1, A2, and B1 are public or private limited-liability companies (see Annex II to Reg. 2157/2001)
- State A, State B, and State S are EU Member States
- A1 and A2:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A
- B1:
  - formed under law of Member State B

  - registered office in Member State B
  - head office in Member State B
- SE:
  - formed under law of Member State S
  - registered office in Member State S
  - head office in Member State S
  - will be covered by the EC Merger Directive

Transactions

- SE:
  - will be regarded as public limited-liability company governed by the law of Member State S
  - acquires holding in A1 and A2
  - such that it obtains more than 50% of the permanent voting rights in A1 and A2
  - in exchange for shares in SE
  - issued to the shareholders of A1 and A2

Questions

1) Assume Member State A is your country

   Tax effects for SH A2 in Member State A

   a) Will the issue of shares by SE to SH A2 in exchange for shares in A2 give rise to any taxation of the income, profits or capital gains of SH A2 or is there roll-over relief?

      According to Art. 2 paragraph 5 of the Decree No. 544 of 1992, the allotment of shares representing the capital of the receiving company to a shareholder of the transferring company in exchange for shares representing the capital of the latter company, does not give rise to any taxation in the hands of that shareholder. The fiscal value of the cancelled shares will constitute the tax basis of the shares received in exchange. Any cash payment received by the shareholder is taxable. [This may constitute a problem since the tax value of the shares is not accordingly increased (see Maisto, The implementation …, p.486)]

   b) Will the answer to the above question be different in the case of:
      i) SH A2 being an individual shareholder not owning a substantial interest?
      ii) SH A2 being an individual shareholder owning a substantial interest?
      iii) SH A2 being an individual entrepreneur?
      iv) SH A2 being a corporate shareholder?

      No, it will not. Note however that a different tax treatment may be applied as regard the cash payment, if any.

2) Assume Member State S is your country

   Tax effects for SE in Member State S

   a) Are there any provisions for the valuation for tax purposes in Member State S of the shares of A1 and A2 acquired by SE? Do the shares have to be valued at the book value of the exchanging shareholder or at a higher value?

      See b) below.

   b) Are there any provisions for the valuation for tax purposes in Member State S of the shares issued to SH A1 and SH A2? Do the shares have to be valued at the book value of the shares exchanged by the shareholder or at a higher value?

      The Decree No. 544 of 1992 requires that at least one of the participants be resident in Italy or that the participation exchanged be effectively connected with a permanent establishment in Italy of a company listed in the Annex to the Directive. It is doubtful whether the term participants ("partecipanti") has to be interpreted as referring only to the shareholders of the acquired company or also to the acquiring company.

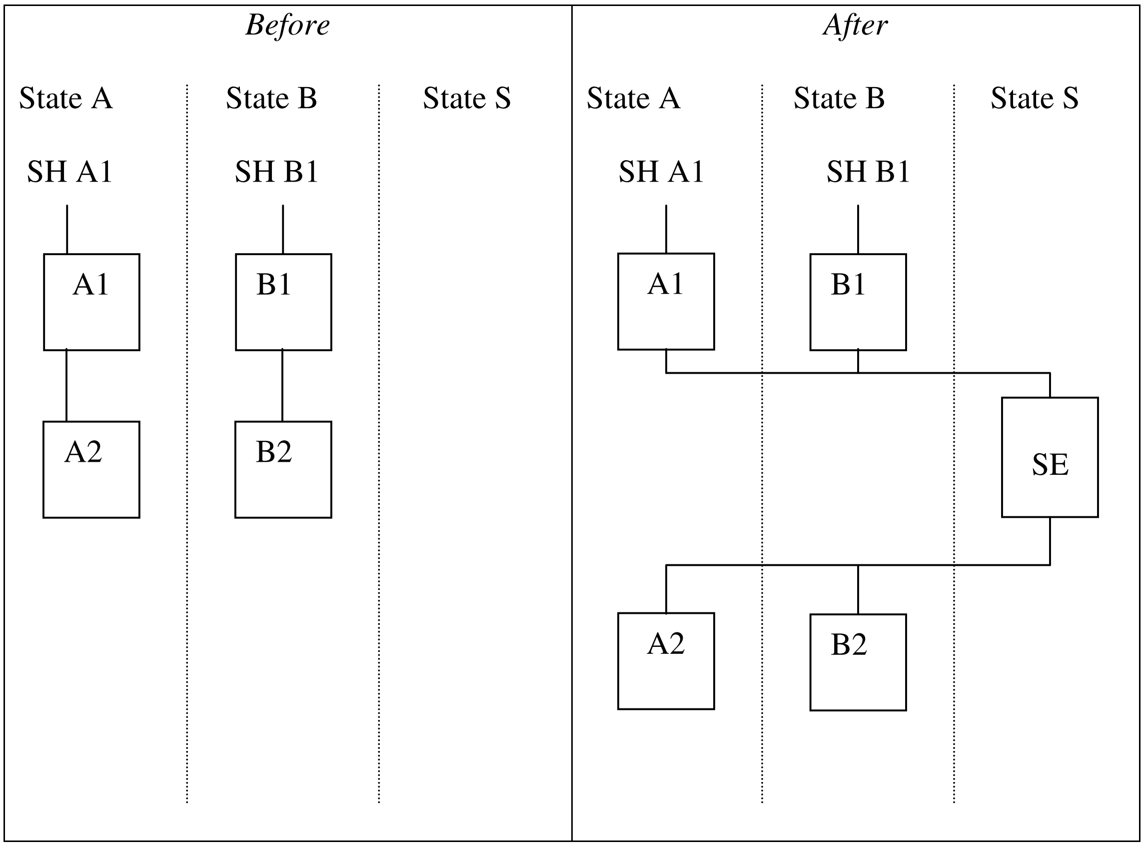
      In the former case, the Decree is not applicable and accordingly the acquiring company may evaluate the received shares at their market value.
      In the latter case, the Decree is applicable. However, even though the Decree in general applies, according to distinguished authors, Art. 2 paragraph 5 does not require that the tax basis of the acquired shares for the acquiring company be the same as that recognized for the participants and consequently the value for tax purposes for the acquiring company is the real value of the shares acquired.

      It may be argued, however, that Art. 2 paragraph 5 applies also to the receiving company and that the exchange of shares is tax neutral and the tax value of the received shares is equal to the tax value of the exchanged shares before the transaction.

CASE 6

Formation of a Subsidiary–SE by exchange of shares

(Art. 2 par. 3(a) jo. Arts. 35 and 36 Reg. 2157/2001)



Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A1, A2, B1, and B2 are existing companies
- SE is a new company
- A1 and B1 are companies or firms within the meaning of Art. 48 par. 2 of the Treaty establishing the European Community or other legal bodies governed by public or private law (Art. 2 par. 3 Reg. 2157/2001)
- State A, State B, and State S are EU Member States
- A1 and A2:
    - formed under law of Member State A
    - registered office in Member State A
    - head office in Member State A
- B1 and B2:
    - formed under law of Member State B

    - registered office in Member State B
    - head office in Member State B

- SE:
    - formed under law of Member State S
    - registered office in Member State S
    - head office in Member State S
    - will be covered by the EC Merger Directive

Transactions

- A1 and B1:
    - *form a subsidiary SE by way of contributing their subsidiaries A2 and B2 respectively to SE*
- *SE:*
    - will be regarded a public limited-liability company governed by the law of Member State S
    - will acquire the shares in A2 and B2 in exchange for shares issued to A1 and B1

Questions

1) Assume Member State A is your country

   <u>Tax effects for A1 in Member State A</u>

   a) Will the issue of shares by SE to A1 in exchange for shares in A2 give rise to any taxation of the income, profits or capital gains of A1 or is there roll-over relief?

      According to Art. 2 paragraph 5 of the Decree No. 544 of 1992, the allotment of shares representing the capital of the receiving company to a shareholder of the transferring company in exchange for shares representing the capital of the latter company, does not give rise to any taxation in the hands of that shareholder. The fiscal value of the cancelled shares will constitute the tax basis of the shares received in exchange. Any cash payment received by the shareholder is taxable. [This may constitute a problem since the tax value of the shares is not accordingly increased (see Maisto, The implementation …, p.486)]

2) Assume Member State S is your country

<u>Tax effects for SE in Member State S</u>

a) Are there any provisions for the valuation for tax purposes in Member State S of the shares of A2 and B2 acquired by SE? Do the shares have to be valued at the book value of the exchanging shareholder or at a higher value?

See b) below

b) Are there any provisions for the valuation for tax purposes in Member State S of the shares issued to A1 and B1? Do the shares have to be valued at the book value of the shares exchanged by the shareholder or at a higher value?

The Decree No. 544 of 1992 requires that at least one of the participants be resident in Italy or that the participation exchanged be effectively connected with a permanent establishment in Italy of a company listed in the Annex to the Directive. It is doubtful whether the term participants ("partecipanti") has to be interpreted as referring only to the shareholders of the acquired company or also to the acquiring company.

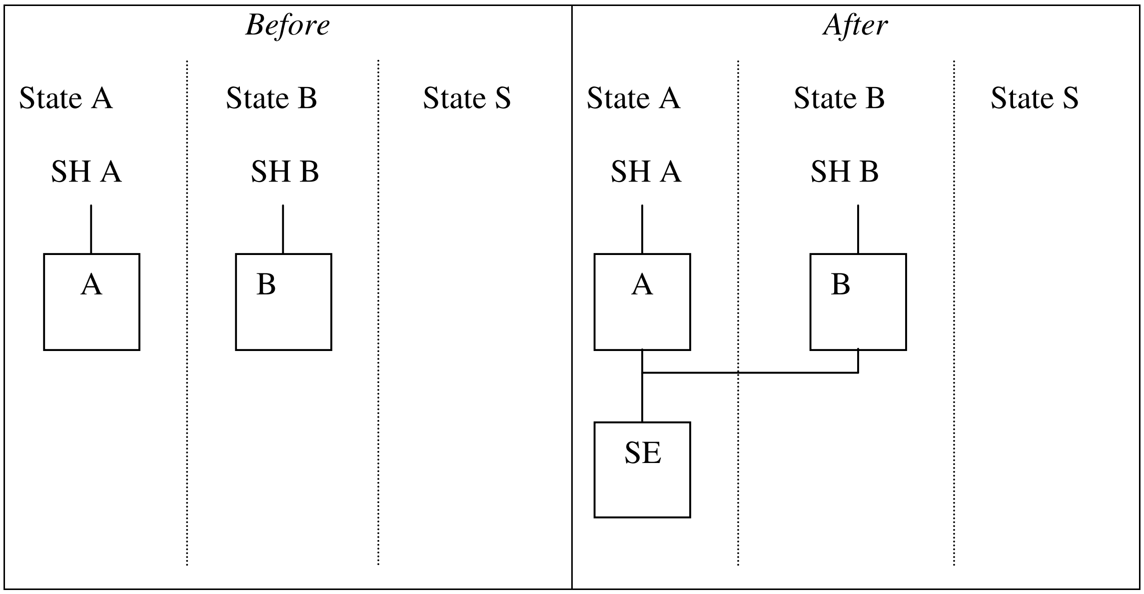
In the former case, the Decree is not applicable and accordingly the acquiring company may evaluate the received shares at their market value.
In the latter case, the Decree is applicable. However, even though the Decree in general applies, according to distinguished authors, Art. 2 paragraph 5 does not require that the tax basis of the acquired shares for the acquiring company be the same as that recognized for the participants and consequently the value for tax purposes for the acquiring company is the real value of the shares acquired.

It may be argued, however, that Art. 2 paragraph 5 applies also to the receiving company and that the exchange of shares is tax neutral and the tax value of the received shares is equal to the tax value of the exchanged shares before the transaction.

CASE 7

Formation of a Subsidiary–SE by contribution of cash

(Art. 2 par. 3(a) jo. Arts. 35 and 36 Reg. 2157/2001)



Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A, and B are existing companies
- SE is a new company
- A and B are companies or firms within the meaning of Art. 48 par. 2 of the Treaty establishing the European Community or other legal bodies governed by public or private law (Art. 2 par. 3 Reg. 2157/2001)
- State A, State B, and State S are EU Member States
- A:
    - formed under law of Member State A
    - registered office in Member State A
    - head office in Member State A
- B:
    - formed under law of Member State B
    - registered office in Member State B
    - head office in Member State B
- SE:
    - formed under law of Member State A
    - registered office in Member State A
    - head office in Member State A
    - will be covered by the EC Merger Directive

Transactions

- *SE:*
  - will take the form of an SE
  - will be regarded a public limited-liability company governed by the law of Member State A
- A and B:
  - form a subsidiary SE

Questions

It is generally assumed that an SE will for domestic corporate income tax purposes be treated as a corporate entity. However, there may be differences between the treatment of an SE and other legal entities, if certain possibilities, e.g. participation exemption or fiscal unity etc. are only allowed between certain types of legal entities and the SE is not yet included. If relevant, please mention some of these situations in your answers to the following questions.

1) Assume Member State A is your country

   Tax effects for A in Member State A

   Will there be any tax effect for A in Member State A as a consequence of the formation of the subsidiary SE in Member State A?

   No, there will not be any relevant tax effect as a consequence of the formation of a subsidiary.

2) Assume Member State B is your country

   Tax effects for B in Member State B

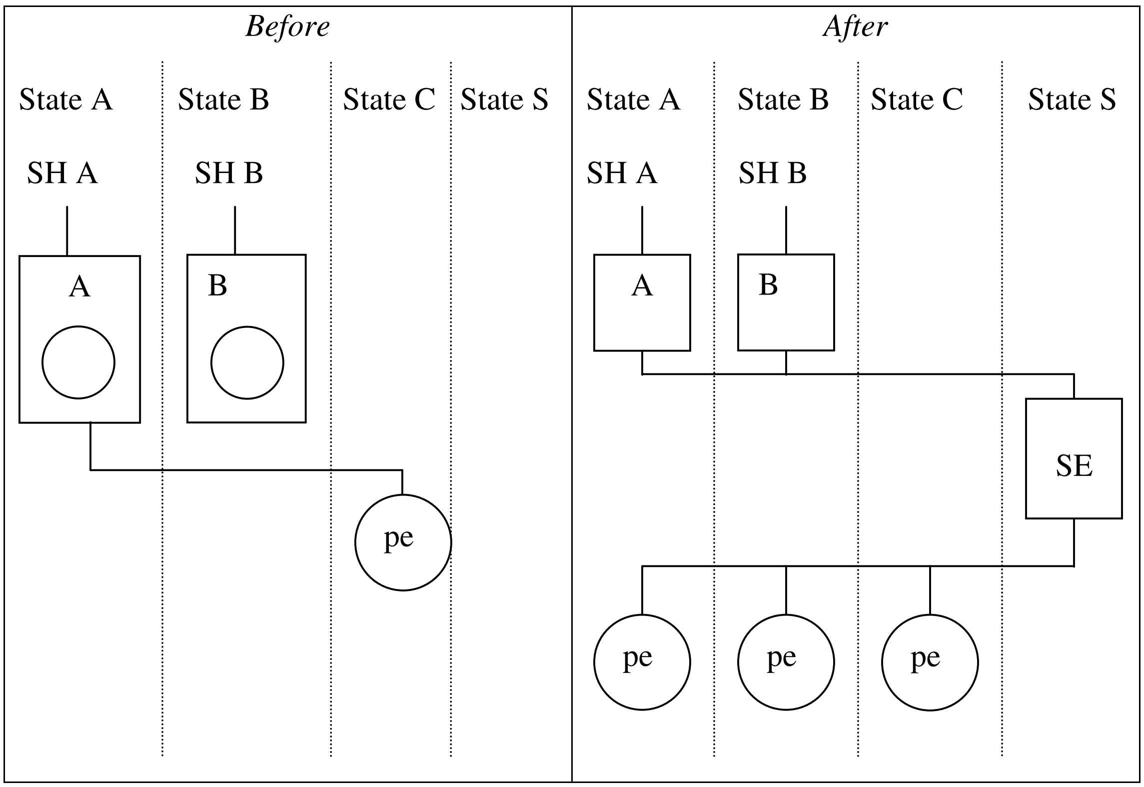
   Will there be any tax effect for B in Member State B as a consequence of the formation of the subsidiary SE in Member State A?

   No, there will not be any relevant tax effect as a consequence of the formation of a subsidiary.

CASE 8

Formation of a Subsidiary–SE by transfer of assets

(Art. 2 par. 3(a) jo. Arts. 35 and 36 Reg. 2157/2001)



Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A, and B are existing companies
- SE is a new company
- A and B are public or private limited-liability companies (see Annex II)
- A and B are companies or firms within the meaning of Art. 48 par. 2 of the Treaty establishing the European Community or other legal bodies governed by public or private law
- A has a permanent establishment in State C
- State A, State B, State C and State S are EU Member States
- A:
    - formed under law of Member State A
    - registered office in Member State A
    - head office in Member State A

- B:
    - formed under law of Member State B
    - registered office in Member State B
    - head office in Member State B
- SE:
    - formed under law of Member State S
    - registered office in Member State S
    - head office in Member State S
    - will be covered by the EC Merger Directive

Transactions

- SE:
    - will take the form of an SE
    - will be regarded a public limited-liability company governed by the law of Member State S
- A (and B):
    - form a subsidiary by way of contributing their branches in Member State A (and B respectively) to SE in exchange for the issue of shares by SE to A (and B respectively)
- A:
    - will transfer its permanent establishment in Member State C to SE in exchange for the issue of shares by SE to A

Questions

1) Assume Member State A is your country

   <u>Tax effects for A and SE in Member State A</u>

   a) Will the transfer of assets give rise to any taxation of capital gains (= real value of the assets and liabilities minus their value for tax purposes) or is there roll-over relief?

      According to Art. 2 paragraph 2 of the Decree No. 544 of 1992, the transfer of assets does not give rise to any taxable gain and the value for tax purposes of the business transferred is carried over to the shares received in exchange. Furthermore, the Decree allows the company transferring the assets to enter the shares received in exchange in its accounting books at their market value at the time of the transfer. In this case, the difference between the market value of the shares and the book value of the transferred asset must be enters into an ad hoc reserve that is taxable upon distribution to the shareholder or upon alienation of the shares received.
      If the assets transferred constitute a permanent establishment in another Member State (in this case in State C), according to Art. 2 paragraph 6 of the Decree No. 544 of 1992, the PE will be considered as if it had been disposed at market value

but a (notional) tax credit will be granted. The credit is equal to the tax that the State where the PE is located would have charged in the absence of the Merger Directive. In this case, the tax value of the shares received in exchange will be increased by an amount equal to the taxable income corresponding to the tax actually due after the credit of the (notional) foreign tax.
Pursuant to the last sentence of Art. 2 paragraph 2 of the Decree No. 544 of 1992, the same rules applicable in case of a merger will apply to this case.
Accordingly, the value that for tax purposes the non-resident receiving company has to attribute to the assets and liabilities of the transferring company is the last tax value the assets and liabilities had before the transfer in the hands of the transferring company. If the acquiring company increases the book value because of the imputation of the merger deficit, a statement has to be attached to the tax return showing the difference between the book value and the tax value of each asset.
Note that, regarding the PE in a third EU State (i.e. State C) of the transferring company (i.e. company A), if the State of the transferring company taxes the capital gain arising from the alienation of the foreign PE, then the tax value of the PE will be equal to its market value]

Moreover, Art. 4 of the Decree No. 358 of 1997 extends the regime applicable to domestic transfers of assets also to EC transfers of assets. In this case, company A could opt for the ordinary regime of taxation of the capital gains as provided for by Art. 54 of the CITA or for the payment of a substitute tax equal to 19% of the capital gain realized. The capital gain has to be computed on the basis of the rule contained in Art. 3 paragraph of the Decree 358, which states that the value at which the assets are deemed to be transferred is equal to the higher of (i) the value of the shares entered in the accounts of the company transferring the assets or (ii) the value of the assets entered in the books of the acquiring company. It is doubtful whether the condition that the assets must have been held for at least three years, as required for domestic transfers, applies also to EC transfers.

b) May provisions or reserves which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State A be taken over with the same roll-over relief by the permanent establishment of SE in Member State A?

Such provisions and reserves can be taken over by the permanent establishment in Italy, provided that they are reinstated in the balance sheet of the Italian post-merger permanent establishment.

According to Art. 3 of the Decree No. 544 of 1992, tax-deferred reserves entered in the last balance sheet of the transferring company not reinstated in the balance sheet of the Italian post-merger permanent establishment of the receiving company are subject to tax in Italy in the hands of the non-resident company.
The above-mentioned provision applies to cases of merger, division and transfer of assets. In this last case, however, the provision should apply only to those

reserves that are effectively connected with the transferred branch of activity, but nothing is stated in the Decree No. 544 of 1992. In this respect some guidance may be found in the Circular Letter No. 98 of 17 May 2000 issued by the Italian Ministry of Finance, according to which relevance should be given to the conditions to which the deferral is related.

c) Are there any provisions in the legislation of Member State A for the valuation for tax purposes of the shares in SE acquired by A?

See answer to a) above.

d) Will SE's permanent establishment in Member State A be allowed to take over the losses of A which have not been exhausted for tax purposes? (If SE would be a company resident in Member State A, would it then be allowed to take over these losses?)

It is doubtful. Art. 4 of the Decree No. 544 of 1992 allows the carry-over of losses to the non-resident receiving company only for the operations referred to in Art. 1 paragraphs a) and b) of the Decree No. 544 of 1992. These paragraphs refer only to the merger or division involving a resident company and another EU Member State resident company. From a literal interpretation of the rule, it seems that such carry-over would not apply to the case under discussion.

If SE, as the receiving company, would be resident in Italy, carry over of losses would also not be possible under Italian legislation.

e) Will Member State A renounce any right to tax the permanent establishment in Member State C?

See answer to h) below.

f) Will Member State A reinstate in the taxable profits of A such losses of the permanent establishment in Member State C as have been set off against the taxable profits of A in Member State A and which have not be recovered (see art. 10 par. 2 of the EC Merger Directive)?

See answer to h) below.

g) Or will Member State A tax profits or capital gains of the permanent establishment resulting from the transfer of assets?

See answer to h) below.

h) If question g) is answered affirmatively, will Member State A give relief for the notional tax charged on these profits or capital gains by Member State C, assuming that Member State C would have levied tax (see art 10 par. 2 of the EC Merger Directive)?

According to Art. 2 paragraph 6 of the Decree No. 544 of 1992, the PE will be considered as if it had been disposed at market value but a (notional) tax credit will be granted. The tax credit is equal to the tax that the State where the PE is located would have charged in the absence of the Merger Directive.

2) Assume Member State S is your country

<u>Tax effects for SE in Member State S</u>

a) What is the value for tax purposes that SE has to attribute to the assets and liabilities of the permanent establishments in Member States A, B and C that is transferred to SE as part of the merger?

There are no rules in the Decree No. 544 of 1992 that deal with this issue. In principle the same rules applicable in case of merger should apply, but nothing is stated in the Decree. The consequence would be that the resident receiving company would be allowed to enter the branches abroad at their market value in its books.

<u>Tax effects for A as shareholder of SE in Member State S</u>

b) Is there any provision in the tax legislation of Member State S that affects A as shareholder of SE?

In principle, the rules on the taxation of capital gains upon transfer of the shares in the Italian company, but exceptions to this taxation are stated in the domestic law and Italy's right to tax is generally restricted by tax treaties.

3) Assume Member State C is your country

<u>Tax effects for A and SE in Member State C in respect of its permanent establishment in Member State C</u>

a) Will the transfer of assets give rise to any taxation of capital gains (= real value of assets & liabilities transferred minus their value for tax purposes) or is there roll-over relief?

The transfer does not result in any taxation in Italy. According to Art. 2 paragraph 2 of the Decree No. 544 of 1992, the assets and liabilities of the PE maintain their pre-merger value for Italian tax purposes.
Moreover, Art. 4 paragraph of the Decree 358 of 8 October 1997 extends the regime applicable to domestic transfers of assets also to EC transfers of assets. Since the transfer of an Italian PE from a EU qualifying company to another EU qualifying company is expressly covered by Art. 1 paragraph 1.d of the Decree No. 544 of 1992, it can be concluded that the domestic regime applies also to this case. Accordingly, company A could opt for the ordinary regime of taxation of the capital gains as provided for by Art. 54 of the CITA or for the payment of a substitute tax equal to 19% of the capital gain realized. The capital gain has to be computed on the basis of the rule contained in Art. 3 of the Decree 358, which states that the value at which the assets are deemed to be transferred is equal to the higher of (i) the value of the shares entered in the accounts of the company transferring the assets or (ii) the value of the assets entered in the books of the acquiring company. It is doubtful whether the condition that the assets must have been held for at least three years, as required for domestic transfers, applies also to EC transfers.

b) May provisions and reserves, which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State C, be taken over with the same roll-over relief by the permanent establishment of SE in Member State C?

It is doubtful. Art. 3 of the Decree No. 544 of 1992 only refers to the tax-deferred reserves and provisions included in the last balance sheet of the resident transferring company. Accordingly, it could be concluded that the non-reinstatement of tax-deferred reserves and provisions in the balance sheet of the non-resident receiving company does not lead to any taxation in Italy, but this conclusion seems not to be in line with the spirit and purpose of the Decree No. 544 of 1992.

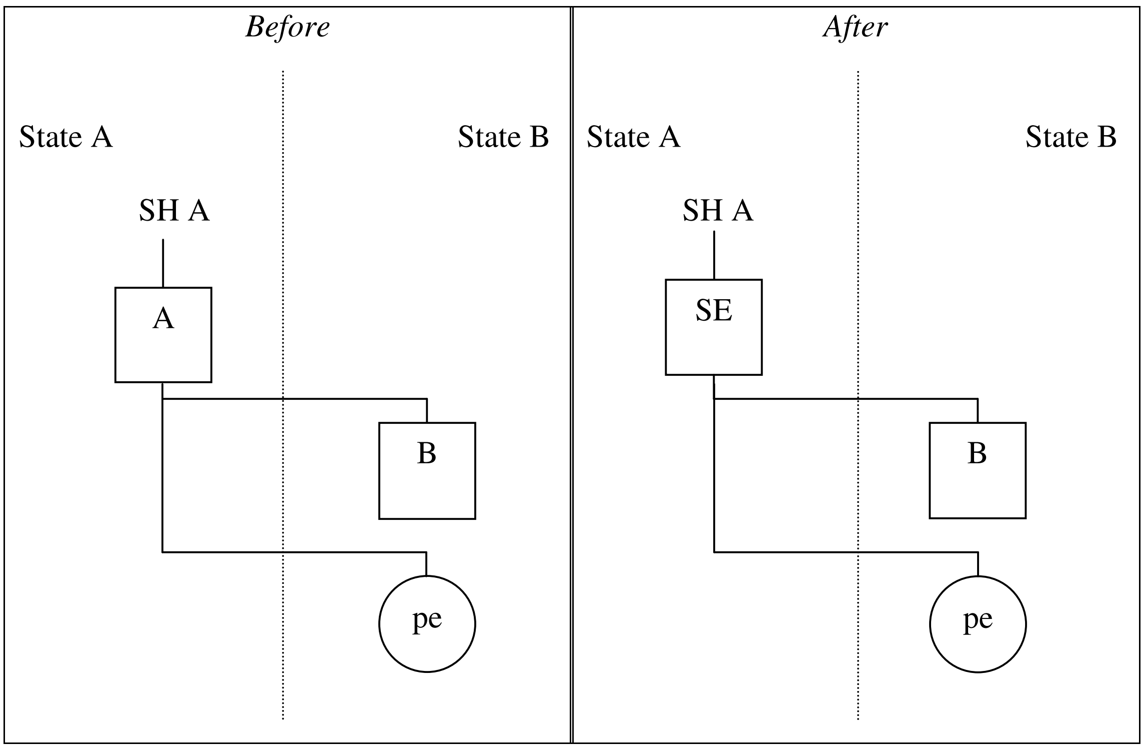
c) Will SE's permanent establishment in Member State C be allowed to take over the losses of A's permanent establishment that have not been exhausted for tax purposes? If SE would be a company resident in Member State C, would it then be allowed to take over these losses?

It is doubtful. Art. 4 of the Decree No. 544 of 1992 allows the carry-over of losses to the non-resident receiving company only for the operations referred to in Art. 1 paragraphs a) and b) of the Decree. These paragraphs relate however only to the merger or division involving a resident company and another EU Member State resident company. From a literal interpretation of the rule, it seems accordingly that such carry-over would not apply to the case under discussion. This is not contrary to the wording of the Directive (Art. 6) but it is certainly against its purpose.

CASE 9

Transformation of public limited-liability company into an SE

(Art. 2 par. 4 jo. Art. 37 Reg. 2157/2001)



Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A and B are existing companies
- pe is an existing permanent establishment
- A and B public limited-liability companies (see Annex I of Reg. 2157/2001)
- State A and State B are EU Member States
- A:
    - formed under law of Member State A
    - registered office in Member State A
    - head office in Member State A
- B:
    - formed under law of Member State B
    - registered office in Member State B
    - head office in Member State B

Transactions

- A will be transformed into an SE, governed by the law of Member State A (Pursuant to Art. 37 par. 2 Reg., the transformation shall not result in the winding up of A or in the creation of a new legal person. However, the Regulation itself does not give guidance with regard to taxation.)

Questions

1) Assume Member State A is your country

Tax effects for A in Member State A

a) Will the transformation of A into an SE give rise to any taxation of capital gains (= real value of assets and liabilities transferred minus their value for tax purposes) or is there roll-over relief for the business carried on in Member State A, or in Member State B through a permanent establishment?

According to Art. 122 of CITA, the transformation will not have any consequences. It is only a change in the Statute of the company, there is neither winding up of the company nor creation of a new company; the company continues to exist but with a different legal form.

b) May provisions and reserves, which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State A, be carried over to SE in Member State A?

See answer to a) above.

c) Will SE be allowed to take over the losses of A that have not been exhausted for tax purposes?

See answer to a) above.

Tax effects for SH A in Member State A

d) Will there be any effect for SH A because of the transformation of its subsidiary company A into an SE?

Since the transformation does not entail winding up of the company and creation of a new company, there will be no effects for the shareholders because of the transformation.

e) Will the answer to question d) be different in the following situations:
   i) SH is a corporate shareholder?

ii) SH is an individual shareholder not owning a substantial interest?
iii) SH is an individual shareholder owning a substantial interest?
iv) SH is an individual entrepreneur?

No.

2) Assume Member State B is your country

<u>Tax effects for the shareholder of B in Member State B</u>

a) Will there be any effect for the shareholder of B because of the transformation of its parent company A into an SE?

Since the transformation does not entail winding up of the company and creation of a new company, it can be concluded that there will be no effects because of the transformation.

<u>Tax effects for A and SE in Member State B</u>

b) Will A be subject to any taxation of capital gains (=real value of assets and liabilities minus their value for tax purposes) or is there roll-over relief?

See answer to e) below.

c) If not, what is the value for tax purposes that SE has to attribute to the assets and liabilities of the permanent establishment in Member State B?

See answer to e) below.

d) May provisions and reserves, which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State B, be taken over with the same roll-over relief by the permanent establishment of SE in Member State B?

See answer to e) below.

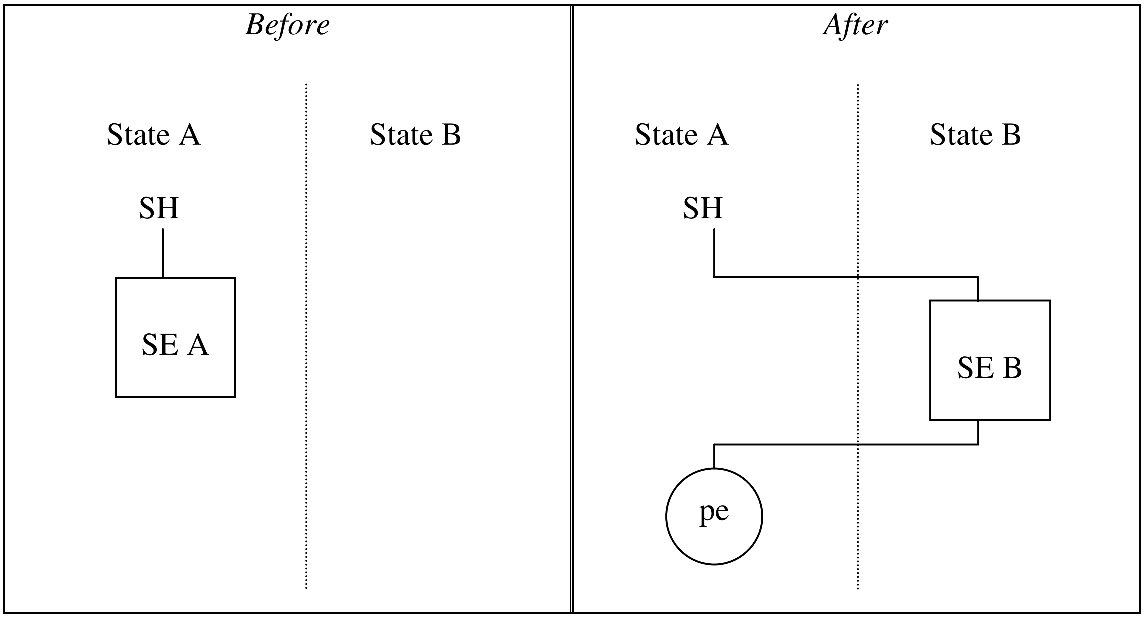
e) Will SE's permanent establishment in Member State B be allowed to take over the losses of A's permanent establishment that have not been exhausted for tax purposes?

Since the transformation does not entail winding up of the company and creation of a new company, it may be concluded that there will be no effects because of the transformation.

CASE 10

Transfer of registered office of an SE

(Art. 8 par. 1 jo. Art. 37 Reg. 2157/2001)



Facts and assumptions

- SE is an existing SE
- State A and State B are EU Member States
- SE A:
  - formed under the law of Member State A
  - registered office in Member State A
  - head office in Member State A
- SE B:
  - statutes are amended to conform to the law of Member State B
  - registered office in Member State B
  - head office in Member State B

Transactions

- registered office and head office of SE are transferred to Member State B (pursuant to Art. 8 Reg. 2157/2001 such a transfer shall not result in the winding up of SE or in the creation of a new legal person)

Questions

1) Assume Member State A is your country

<u>Tax effects of the transfer for SE</u>

a) Does the transfer entail a winding up of SE for tax purposes?

It should not. However, there are no rules explicitly stating that.
Some Italian commentators (Mayr, Effetti del trasferimento della sede all'estero, in Corr.Trib. 39/95,p. 2707) believe that the rule contained in Art. 20bis of the CITA proves that the transfer of the residence to another Country does not involve a winding up of the company. Civil law literature tends, however, to consider the case a winding up for civil law purposes. Due to the fact the Regulation No. 2157 of 2001 (Art. 8) explicitly states that the transfer shall not result in the winding up of the SE or in the creation of a new legal person, then it may be concluded that the transfer of the residence to another Country does not involve a winding up of the company for Italian tax purposes.

b) What are the tax consequences in case of a winding up of SE?

See a) above.

c) Does it make a difference whether or not a permanent establishments of SE B remains in Member State A?

Yes, it does. According to Art. 20bis paragraph 1of the CITA, the transfer of the registered seat or of the civil law residence, which determine the loss of the Italian fiscal residence, involves the realization at market value of the business, unless it constitutes a permanent establishment in Italy.
If the Italian company had a permanent establishment abroad, it is deemed to have transferred it at market value. Note that, different from the case of an EC merger, Italy will grant a credit only for taxes definitively paid in the Country where the permanent establishment is situated.

d) If after the transfer of the registered office, SE B will have a permanent establishment in Member State A, can SE B take over the provisions and reserves which are partly or wholly exempt from tax with the same roll-over relief?

According to Art. 20bis paragraph 2 of the CITA, tax-deferred reserves, including those taxable upon distribution, that are not reinstated in the books of the resulting permanent establishment will be subject to tax in Italy.

e) If after the transfer of the registered office, SE B will have a permanent establishment in Member State A, can SE B's permanent establishment in

Member State A take over the losses of SE A that have not been exhausted for tax purposes?

There is no provision that deal with this issue. It can probably be concluded that losses carry-forward is not allowed in this case.

<u>Tax effects of the transfer for SH</u>

f) What are the tax effects for SH in case the transfer results in a winding up of SE for tax purposes?

See answer i) below.

g) Is the answer to 1f) different if:
   i) SH is a corporate shareholder?
   ii) SH is an individual shareholder?
   iii) SH is an individual not owning a substantial interest?
   iv) SH is an individual owning a substantial interest?
   v) SH is an individual entrepreneur?

   See answer i) below.

h) Are there any effects for tax purposes if the transfer of the registered office is not considered as a winding up for tax purposes?

   See answer i) below.

i) Is the answer to 1h) different if:
   i) SH is a corporate shareholder?
   ii) SH is an individual shareholder?
   iii) SH is an individual not owning a substantial interest?
   iv) SH is an individual owning a substantial interest?
   v) SH is an individual entrepreneur?

   As stated in answer a), the transfer should not result in the winding up of the company.
   Unfortunately, Art. 20bis of the CITA only deals with the issues arising at the level of the company but nothing is stated as regards the shareholders.
   In this respect, the result will be different depending on the residence and on the characteristics of the shareholder. If the shareholder is resident in Italy, then he will lose the right to the imputation credit granted upon distribution of dividends by a domestic company. Furthermore, if the shareholder is a company qualifying for the 95% exemption (either under domestic law or under EC parent-subsidiary directive), then Italy may not tax the profits distributed by the non-resident SE to the resident company.
   If the shareholder is a non-resident, Italy will lose its right to apply withholding tax upon distribution of profits.

2) Assume Member State B is your country

   Tax effects of the transfer for SE

   a) If SE is considered to be a new company, how should the assets and liabilities of SE be valued?

      There are no rules dealing with this issue. The possibilities are two: either the historical cost or the market value. The only rule that might have some bearing in this case is Art. 77 paragraph 3bis of the CITA, which states that the tax value to be attribute to assets used for business purposes, which come from the personal assets of the entrepreneur, is the historical cost.

   Tax effects of the transfer for SH

   b) Are there any tax effects for SH in case the transfer results in a formation of a new SE in your country? For example, with regard to the valuation of the shares in SEB?

There are no rules dealing this issue. Due to the fact the Regulation (Art. 8) explicitly states that the transfer shall not result in the winding up of the SE or in the creation of a new legal person, then it may be concluded that the tax value of the shares in SEB will be equal to the tax value the shares had before the transfer. Note however that the (eventual) withholding tax levied by the State where the company distributing the dividends is resident may be different.