



Real Estate Investment in Italy

THE LEGAL PERSPECTIVE



Introduction

The Italian real estate market spiked in 2017, hitting a record figure of EUR11 billion in 2017. In spite of political turmoil affecting Italy and other European countries the market is still very hectic.

Much of the investment appetite comes from new investors which had not previously targeted the Italian market, while more traditional investors still have strong interest for the Italian market. The NPL-UTP markets have still many unexplored investment pockets. Yield expectations hit a record low for office spaces in Milan and high-street retail.

This scenario requires a highly specialized approach and, in this respect, real estate is a key practice area for DLA Piper. Our sector approach provides our clients with the highest level of legal assistance in respect of all the areas involved in real estate investments such as, town planning, environmental, corporate, finance, tax, restructuring and investment funds.

This guide provides an overview of how the legal system in Italy operates and is aimed at covering the basics relating to investing in the Italian real estate market as a foreign investor. It is intentionally not an exhaustive guide.

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1. Ownership of real estate

1.1 Property rights

In Italy there are various types of rights relating to real estate assets:

- Absolute freehold or full ownership (*piena proprietà*) – the right to fully and exclusively enjoy and dispose of the property: the broadest right which may be held in real estate.
- Right to build (*diritto di superficie*) – the right to build and maintain a building on or underneath a third party's property, granted for a specific period of time. When this expires the landowner becomes the legal owner of the building. It is also possible to sell the title to a building without owning the title to the underlying land (where the seller is a public authority the sale will be for a maximum 99-year term).
- Beneficial interest (*diritto di usufrutto*) – the right to enjoy a third party's real estate for a specific period of time. This cannot be longer than the lifetime of the beneficiary if they are an individual, or more than 30 years if the beneficiary is a legal entity. The beneficiary can use the real estate in the same way as an owner, including having the right to collect interest or to grant leases, provided the original use is maintained.
- Right of use (*diritto d'uso e di abitazione*) – the right to use real estate in order to meet the needs of the person holding the right and those of their immediate family.
- Emphyteusis or long lease (*diritto di enfiteusi*) – a right to enjoy a property owned by a

third party with rights similar to those granted to the full owner. The leaseholder pays a rent to the bare owner, must enhance the property and is granted the right to become full owner by paying a certain amount. This right may be perpetual and its duration cannot be less than 20 years. This right is rare in common practice.

- Easement (*servitù*) – an encumbrance (*onere*) burdening a property in order to provide another property, owned by a different person/entity, with a direct advantage (*utilità*). These rights are all classified as in rem rights (*diritti reali*), as further detailed below.

1.2 Co-ownership and condominium

Property rights, including the right of full ownership of real estate, may be co-owned by two or more persons, companies and/or other legal entities.

Co-ownership can also take the form of condominium: usually in relation to housing but also, in certain cases, to shopping malls where different units in the same building and/or different buildings in the same real estate complex are owned by different owners but some of the areas and services are used by the owners collectively.

The members of the condominium have a right of co-ownership over the common assets which are proportionate to the value of their respective interests in relation to the value of the entire building/

real estate complex. The rights of co-ownership in a condominium are expressed in *millesimi* (i.e. participation interests calculated on the basis of 1/1,000) and listed in a millesimal chart; the millesimal quota represents the value of the voting rights of each member of the condominium.

The co-owners may adopt condominium regulations (mandatory where there are more than ten co-owners) laying down rules governing, for instance, the use of the common areas and the common plant, the allocation of relevant expenses and the management of the condominium.

The right of co-ownership may only be transferred together with a transfer of the owner's interest.

1.3 Restrictions

In general, there are no restrictions on the purchase of real estate assets by foreign investors. However, where an investment is by way of the purchase of shares in a corporate vehicle, there are certain restrictions that may be imposed by the Foreign Ministry (*Ministero degli Affari Esteri*).

In rare cases mandatory pre-emption rights apply to the sale of real estate assets. (See paragraph 3.3 Pre-emption rights).

There are other restrictions on sales by an individual in a family context.

2. Acquisition of ownership

Investments in real estate in Italy can be made in various forms. There are two main alternative structures available:

- asset purchase; and
- acquisition of shares in the asset-owning corporate vehicle (i.e. a share purchase).

2.1 Formal requirements

A deed of transfer must be made in writing and authenticated by a public notary in order to be filed (*trascritto*) with the Real Estate Register (*Conservatoria dei Registri Immobiliari*).

Preliminary contracts must take the same form as the final deed of transfer and therefore must also be in writing.

The content of the contract is negotiable but must include the price; the identity of the property or of the quotas/ shares to be transferred in the case of a share purchase; details of the relevant building permits; and rules regarding the allocation of risks and benefits relating to the property.

When the contract is signed in front of a public notary, the means of payment, details of the real estate agent involved and the agency fee must be indicated in the notarial deed.

2.2 Registration

Although it is not a requirement for validity, deeds are usually filed with the publicly available Real Estate Register (*Conservatoria dei Registri Immobiliari*) held by each municipality. This avoids conflicts with future buyers and third parties.

The register records information relating to the property, including sales and purchases, mortgages, easements, rights of use and all the in rem rights, as well as any pending disputes.

An *in rem* right, including the right of full ownership, is not effective against the person who effected a filing (*trascrizione*) on the property if it is registered after the filing of that person's right, even if the relevant right was acquired earlier.

A filing can benefit from these rules only if the previous acquisition deed has also been properly filed (the rule of continuity of filings, i.e. an uninterrupted chain of ownership).

Preliminary agreements relating to an existing property or to a property under construction can also be registered in order to protect the buyer against any subsequent filing of third parties' rights or a second sale of the same asset. This protection stops one year after the completion date specified in the preliminary agreement and, in any event, three years after the registration of the preliminary agreement.

The filing of a preliminary agreement does not have the same effect as a final agreement, but it gives retrospective effect to the final agreement as from the date of filing of the preliminary agreement (the booking effect – *effetto prenotativo*).

Real estate is also registered in the Cadastre Register, which is held by the municipality in which the property is located, and consists of the Land Cadastre, in which

undeveloped land is recorded, and the Building Cadastre in which buildings are recorded. Both land and buildings must be registered and after registration are attributed a cadastral income. This forms the basis for calculating the municipal property tax (IMU-IUC see paragraph 7). Cadastral income can be subject to review by the relevant authority.

2.3 Asset deals

Investors usually prefer asset deals, since they do not carry any risks not directly related to the property and allow the real estate to be acquired without further material or people.

In Italy an asset deal may be structured as: (a) an acquisition of a real estate asset; or (b) an acquisition of an ongoing business.

In the purchase of an ongoing business, the purchaser is legally obliged to step into existing contractual relationships and to take over certain liabilities as part of the public law authorization for the carrying on of the business.

Usually, the parties to the transaction enter into an agreement such as a letter of intent or heads of terms, providing the potential buyer with an exclusivity period in which to carry out the due diligence.

Before buying a property it is necessary to be aware of:

- its history;
- the legal title held by the seller, and any defects or problems with it;
- planning permissions that allowed it to be built;
- agreements with neighbors;
- possible encumbrances;
- environmental issues; and (for ongoing business sales):
- commercial authorizations and other necessary public permits; and
- all the contracts concerning the business, including employment agreements.

Normally, public notaries carry out a search on title in the Real Estate Register. The notary's report is usually part of the legal due diligence and includes an investigation into the existence of any third party rights as well as the seller's title to the property. An investor will usually appoint a notary public to provide an updated 20 year notarial report (*relazione notarile ventennale*), which is the only document giving legally conclusive evidence of legal title to the property and the relevant encumbrances.

Title insurance is new in Italy, and not common practice.

Generally it is for the buyer to satisfy itself about the issues covered in due diligence but the seller can be asked about key issues of concern which may affect the value, occupation or use of the property.

Misrepresentation by the seller may lead to cancellation of the agreement, the payment of damages, a reduction in the price or, where appropriate, the seller being required to rectify any specific defects.

By law, the seller guarantees that it has title to the property, and that the property is free from any third-party rights and from any defects that might prevent the agreed use of the property or have a negative impact on its value. Breach entitles the buyer to request the termination of the agreement with a full refund of the price, as well as payment of any additional damages. Alternatively, the buyer may ask for a reduction in the price. Breaches must be notified within eight days of discovery and a one-year limitation period applies from the date the buyer takes possession of the property.

Most statutory warranties are negotiable. Current practice is to limit the extent of the warranties and to place more importance on the role of due diligence by excluding liability for any issues disclosed through due diligence.

In new property the buyer has a ten-year warranty under statutory law. The developer is liable if the structure collapses or suffers from serious defects.

2.4 Share purchases

A vendor may want to obtain specific tax benefits by selling the shares of the corporate vehicle instead of selling the property directly. Most double tax treaties signed by Italy exempt the profit derived from the sale of shares from taxation in Italy if the selling shareholder is not tax resident in Italy.

It may also be that the corporate vehicle was used for development activities and that the vendor wishes to transfer all liabilities deriving from the development to the purchaser by selling the corporate vehicle as such. Sales of the corporate vehicle instead of the property itself are becoming increasingly popular in the Italian real estate market.

In these situations, it is highly advisable for the investor to appoint professionals in order to carry out legal and technical due diligence covering all legal aspects relating to the shares of the target company, existing debts, receivables, liabilities, contracts executed by the target company, financial statements, and the company books.

In relation to the corporate governance of Italian corporate vehicles, be aware of the following:

- In a limited liability company (Srl) considerable flexibility can be agreed in the by-laws and voting and profit rights can be freely allocated. The holders of the quotas can appoint and remove directors and may also have approval rights over management decisions. The directors are responsible for day-to-day business decisions. The company can be managed by either a sole director or a board of directors. A board of statutory auditors is required if (i) certain thresholds relating to turnover and number of employees are exceeded for two years, or (ii) the Srl is required to prepare consolidated financial statements, or (iii) the Srl is the controlling entity of a company which is subject to accounting control. Unless the contrary is stated in the articles of incorporation the Srl will be audited by a single statutory auditor.
- In a joint stock company (SpA) different categories of shares with different rights can be created. Voting and profit rights can be freely allocated. An SpA can be managed in any of the following ways: (i) by a sole director or a board of directors appointed by the shareholders meeting (the traditional system); (ii) by a supervisory board and

a management board (the two-tier system); or (iii) by a board of directors appointed by a shareholders' meeting and an executive committee of the board (the one tier system). The appointment of statutory auditors is mandatory. The shareholders may choose to appoint a board of statutory auditors comprising either three or five permanent members, in which case two alternate members must also be appointed.

2.5 Real estate investment funds and SICAFs

2.5.1 REAL ESTATE INVESTMENT FUNDS

Real estate investment funds (*fondi di investimento immobiliare*) are quite common as an instrument to invest in real estate assets, especially by institutional investors.

According to the Directive 2011/61/EU on alternative investment fund managers (AIFMD) and to the Legislative Decree 58/1998 – the so-called Unified Financial Act, (UFA), an Italian real estate investment fund is a closed end alternative investment fund (AIF), i.e. it is a scheme established and managed by a manager as a segregated pool of assets divided into units and collected, through one or more issues of units, among a plurality of investors, managed as a whole in the interest of the unit holders and independently from them. It is invested mainly in real estate on the basis of a predetermined investment policy.

An Italian real estate investment fund whose units can be subscribed (or purchased) only by professional investors and by the other investors identified by the Decree of the Ministry of Finance no. 30 of March 5, 2015 is described as reserved.

A reserved real estate investment fund may be established and managed by an Italian management company which is licensed by the Bank of Italy or by an authorized entity resident in an EU Member State.

Italian reserved real estate investment funds must be managed in accordance with a predetermined investment policy and must:

- invest an amount equal at least to two-thirds of their total value in: (i) real estate assets; (ii) rights *in rem* over real estate assets (iii) equity interests in real estate companies (*società immobiliari*); (iv) other real estate AIFs; and
- invest any remaining third of their total value in other legally permissible assets.

They cannot directly carry out any building activity.

There are risk concentration rules aimed at limiting the stable investment of the fund's assets in single properties. These risk concentration limits can be derogated from in the case of reserved funds, but a de facto minimum level of diversification of risks must be ensured.

Investors participate in a real estate fund by subscribing or purchasing units. Several unit classes can be issued, provided that investors subscribing the same unit class are granted the same powers and duties.

2.5.2 SICAF

An Italian real estate SICAF is a closed-end AIF under the AIFMD and the UFA, i.e. it is a scheme established as a joint stock company (SpA) with fixed capital and a registered office located in Italy, having as its exclusive corporate purpose the investment of the assets collected through the issue of shares (or other equity instruments), among a plurality of investors, managed as a whole in the interest of its investors and independently of them.

It is invested mainly in real estate on the basis of a predetermined investment policy.

SICAFs are subject, in general, to the same regulations provided for other AIFs with respect to, inter alia, investment activity, risk concentration limits, plurality of investors, etc., of course adjusted to the different nature of the SICAF (i.e. an AIF constituted under statute) as opposed to other AIFs constituted under the law of contract.

The establishment of a SICAF must be authorized by the Bank of Italy.

3. Other rights to property

3.1 Mortgages, pledges, privileges

A mortgage (*ipoteca*) is an *in rem* security which burdens real estate assets and, in particular, it is the most common form of security over real estate (which includes the land, buildings erected on it and fixtures which form part of those buildings).

The creditor holding a receivable secured by a mortgage is entitled to start an expropriation (*espropriazione*) in respect of the burdened property. Following the enforced sale, the proceeds are distributed among all creditors in the enforcement procedure, after prior payment of the beneficiary of the mortgage.

A mortgage may burden not only the right of full ownership over real estate, but it may be established also over certain other real estate rights, eg rights to build (*diritti di superficie*), beneficial interests (*diritti di usufrutto*), bare ownership (*nuda proprietà*).

A mortgage may be established by means of a voluntary deed of the debtor (or of a third party over its properties) (*ipoteca volontaria*) but in certain cases the law expressly entitles a creditor to establish a mortgage over the properties of the debtor (*ipoteca legale*), most importantly the right granted to a seller of a real estate asset in order to secure the payment of the price.

Mortgages must be executed by deed in front of a Notary Public and must be filed (*iscritta*) with the relevant Real Estate Register in order to be validly established.

Judicial awards and orders of payment issued by a court entitle the creditor to establish a mortgage over the properties of the debtor (*ipoteca giudiziale*). Establishment of the mortgage will be valid upon filing with the Real Estate Register.

A property may be burdened by more than one mortgage, in which case, a claim regarding the credit secured by the senior mortgage (first ranking mortgage) has priority over those concerning receivables secured by junior mortgages established subsequently (classified as mortgages of second ranking, third grade, fourth grade etc.).

Being an *in rem* right, mortgages do not terminate automatically in the event of transfer of the properties burdened by the same, indeed they “follow” the property and stay with the same (so-called *ius sequelae*).

Unlike a mortgage, a pledge (*pegno*) is an *in rem* security which burdens only movable assets and not real estate assets. Finally, various claims, collectively referred to as privileges (*privilegi*) have statutory priority against the claims of other creditors in relation to the proceeds of a debtor’s property, e.g. the state for direct and indirect taxes.

In principle, pledges prevail over privileges over movables, and special privileges over real estate assets and immovable properties prevail over mortgages.

3.2 Easements

An easement (*servitù prediale*) consists of an encumbrance (*onere*) burdening a property in order to provide another property, owned by a different person/entity, with a direct advantage (*utilità*); indeed

easements require the existence of a relationship between two properties, the burdened one (*fondo servente*) and the benefited one (*fondo dominante*), without prejudice to the possibility of establishing reciprocal easements between the burdened properties.

A non-exhaustive list of the most common type of easements includes rights of way (*servitù di passaggio*) which could be with vehicles and/or pedestrian (*carraio e pedonale*) and which generally allow passage through part of one property to reach another, electric pipeline easements (generally in order to allow the main electric operators to place, maintain and operate electric booths and pipelines for the distribution and supply of electricity); gas pipeline easements, etc.

Being *in rem* rights, easements can be enforced vis-à-vis third parties, and they do not terminate in the event of the transfer of the properties affected (adversely or usefully) by the same, indeed they “follow” the property and stay with the same (*ius sequelae*).

Typically easements are established by means of a contract entered into by the owners of two properties, but they could be also established by means of an administrative measure or judicial awards.

The agreements which establish easements must be in writing and, in order to be effective vis-à-vis third parties (e.g. the purchaser of the affected properties), must be executed by means of a notarial deed and filed (*trascritti*) with the Real Estate Registers.

It is also possible to affect a property by establishing personal rights over the property in favor of a person/entity, rather than in favor of another real estate asset. Such rights would be not considered as *in rem* rights, but as personal rights (*diritti personali*), not enforceable vis-à-vis third parties and having no automatic *ius sequelae* in the case of a transfer of the affected property.

For an investor it is advisable to determine whether any easements adversely affect the target property, or whether the latter property is granted easements in its favor or also. Consideration must also be given to whether the implementation of a planned investment such as the development of land or the enhancement of a shopping mall requires the establishment of easements in favor of the purchased property.

3.3 Pre-emption rights

In rare cases mandatory pre-emption rights apply to the sale of real estate assets.

In the case of commercial lease agreements (lease agreements for non-residential use) tenants carrying out activities involving direct contact with the public (as users and consumers) have a pre-emption right if the landlord intends to sell the property they are leasing during the term of the lease; in particular, tenants are entitled to purchase the premises on the same terms and conditions.

In Italy some real estate assets are considered protected because of their historical or landscape value. In this case the building or area will be subject to a number of legal burdens, and any work involving the property is subject to the prior authorization of the competent public authority (*Soprintendenza*). Moreover, the state has a pre-emption right over properties with historical or landscape value. Deeds of conveyance relating to such properties therefore have to be mandatorily served on the relevant public authority and are conditional upon the exercise of the state's pre-emption right.

Furthermore, in the event of a transfer of agricultural land which are let to small independent farmers (*coltivatori diretti*) pursuant to a lease of agricultural land, the lessee is granted a pre-emption right (agricultural pre-emption right), provided that certain requirements are met. In addition, the agricultural pre-emption right is also granted to direct farmers owning adjoining land.

3.4 Condemnation (compulsory purchase)

Condemnation is possible but only where specific permission is granted in accordance with the law. Moreover, expropriation is only allowed if this is in the public interest and in such cases the state must pay compensation to the parties involved.



4. Zoning and planning law permits

In Italy, different levels of government (20 Regions, 103 Provinces, over 8,000 Municipalities) have land use planning tasks assigned to them. The state is responsible for guidance and coordination. As a consequence, town planning regulations are structured on four different levels: (i) the State, (ii) the Region, (iii) the Province and (iv) the Municipality.

The State sets the general rules and guidelines for planning and building law which are then implemented on a regional, provincial or municipality level.

The Municipalities are the central point in the definition of programmes for development and transformation of land. They approve the General Town Planning Instrument (which has different names, depending on the regional laws).

Each building must be compliant with the General Town Planning Instrument provided at municipal level.

As to the designated use, buildings constructed legitimately before the coming into force of the General Town Planning Instrument are legitimate even if not in compliance with the new General Town Planning Instrument and can be maintained, but not modified.

Changes in use that involve a transfer from one use category to another (the principal categories are: residential, commercial, industrial, offices) require the issuing of a building title and the payment of related fees. On the other hand, changes that involve a change within the same category and that do not need main refurbishment works do not require any fee payment.

Generally speaking, any construction activity is subject to a building title. There are three types of building titles (minor works do not need a building title but the Municipality must be notified):

- the building permits, i.e. administrative licenses issued by the Municipality
- the SCIA – certified declaration of commencement of works (*segnalazione certificata di inizio attività*), i.e. a communication filed by the developer with the Municipality (and signed by an architect or an engineer, who shall attest that the works to be carried out are compliant with relevant regulations) and by means of which the developer merely communicates to the local competent administration its intention to begin the construction works.

Works can be started immediately after the filing, save for the power of the Municipality to control the existence of the legal requirements to perform the declared activities, in the subsequent 30 days

- the CILA communication of commencement of works (*comunicazione di inizio lavori asseverata*), i.e. an instrument similar to the SCIA, related to works with a minor impact

Building titles related to new buildings or refurbishment works (*ristrutturazione edilizia*) are subject to the payment of a fee (contribution on construction cost) to the Municipality.

Buildings of historical or landscape value are subject to special rules.

Under Italian law, in order to carry out retail activity the operator needs a trade license granted by the Municipality or by the Region, depending on the sales area.

5. Environmental liability

Italian legislation, specifically Legislative Decree 152/2006 (the Environmental Code), provides for a list of developments with a potential impact on the environment:

- In the case of developments requiring a variance to the General Town Planning

Instrument a strategic environmental evaluation (VAS) aimed at verifying the sustainability of the plan or program from an environmental point of view is needed.

- For developments with a potential impact on the environment, an environmental impact

evaluation (VIA) whose main purpose is to provide an overall assessment of the environmental impact of each project and of their execution, is needed.



6. Leases

6.1 General overview

Commercial lease agreements can be:

- property lease agreements (*contratti di locazione*); or
- business lease agreements (*contratti di affitto d'azienda*).

6.2 Property lease agreements

Property leases are generally divided into (i) non-residential (also referred to as commercial) leases i.e. for offices, retail space, hotels, etc.); and (ii) residential leases.

The Italian Tenancy Law contains certain mandatory provisions (e.g. relating to the term of the lease, rent increases, tenant's rights to sublet and assignment, etc.) that may not be departed from in favor of the landlord, but only in favor of the tenant. Any contractual deviation from these which is less favorable to the tenant, even if explicitly accepted, would be declared null and void and automatically replaced by the mandatory provision of the Tenancy Law.

As regards non-residential lease agreements entered into after November 11, 2014 (and pre-existing leases subject to amendment agreements) with a yearly rent higher than EUR250,000 (excluding those regarding buildings with a historical value confirmed by a local administrative order), the parties are free to expressly agree terms and conditions which depart even if they favor the landlord from the mandatory provisions of the Tenancy Law.

Since the execution of a business lease agreement instead of a property lease agreement traditionally relied on the wider freedom granted to the parties in the negotiation of the contractual terms and conditions, it is clear that this advantage currently only applies to non-residential lease agreements with a rent to equal or lower than EUR250,000.

6.3 Business lease agreements

If the leased assets are a going concern or business branch (*azienda or ramo d'azienda*), and the parties execute a business lease agreement, the above-mentioned mandatory provisions of the Tenancy Law do not apply.

The choice to use either a going concern or a property lease contract is also based on the type of business activity carried out by the relevant operator. Property lease contracts are used either (a) when specific individual pre-requisites are required by the applicable laws and regulations for the issuance of the relevant trade authorization and such pre-requisites do not exist in relation to the landlord only; or (b) when the activity carried out does not require a trade authorization (such as, by way of example, the following service activities: banks, pharmacies, solariums, beauty centers, hairdressers etc.). Pursuant to section 2555 of the Italian Civil Code and the relevant Court holdings, a going concern is a unitary and organized complex of movable and immovable assets, linked by an interdependence and complementary relationship, which are necessary to carry out the enterprise.

In any case, should a business lease agreement not actually have as its object a genuine going concern, the risk is that it may be re-classified as a property lease agreement, to which the mandatory provisions of the Tenancy Law apply.

A further risk is in relation to the employees that may be hired by the lessee during the lease. According to mandatory provisions of law, the employment contracts in place upon expiration or termination of the contract would be automatically transferred to the lessor.

6.4 Main terms and conditions in lease

6.4.1 DURATION

A minimum term of six years applies for commercial leases (except where the activity to be carried out in the premises is temporary) and nine years for hotel leases. If the parties agree a term lower than the legal minimum, the term is automatically replaced by the minimum statutory term. Parties are free to agree longer leases.

Upon expiration the contract is automatically renewed on the same terms and conditions for another term unless either party gives notice not to renew at least 12 months (or 18 months in the case of hotels) in advance. On the first expiration the landlord can only refuse to renew in very limited circumstances, while at the end of the second term there are no restrictions on the landlord's right to refuse a renewal.

This minimum duration and the provisions concerning automatic renewal of the lease may be departed from if the yearly rent exceeds EUR250,000.

Residential leases must have a minimum term of at least four years. When the initial term expires these leases are automatically renewed for a further period of four years on the same conditions, unless the parties agree otherwise.

6.4.2 WITHDRAWAL

The landlord is not entitled to withdraw from the property lease agreement before the expiration date and any contractual withdrawal right in favor of the landlord would be inconsistent with the Tenancy Law and, therefore, null and void.

The tenant is entitled to withdraw from the property lease agreement before the expiration date if there are serious reasons (*gravi motivi*) by giving six months' prior notice; the parties may also provide the tenant with a contractual withdrawal right, entitling the same to freely withdraw from the lease agreement before its expiration. The serious reasons have been defined by case law and may be summarized as unforeseeable, subsequent events outside the control of the tenant.

These restrictions do not apply if the yearly rent exceeds EUR250,000.

6.4.3 RENT AND RENT REVIEW

The parties are free to determine the amount of the rent.

According to the Tenancy Law, rents may be adjusted annually by a maximum of 75% of the variation in the ISTAT index (a measure of consumer price inflation) (or 100% where the duration of the

lease exceeds the minimum term provided for by law).

These limitations do not apply if the yearly rent exceeds EUR250,000.

6.4.4 OPERATING EXPENSES

Generally, expenses for any common services provided by the landlord are paid by tenants in proportion to the size of their units relative to the total rentable area of the property.

The costs of the utilities are usually paid by tenants on the basis of their specific usage and requirements.

6.4.5 MAINTENANCE, REPAIR AND RENOVATION AT END OF LEASE

Generally the tenant is responsible for minor repairs and ordinary maintenance while the landlord is responsible for extraordinary maintenance, unless otherwise set out in the contract. In any case, according to the prevailing case law, the costs of extraordinary maintenance of the structural parts of the property are borne by the landlord.

The tenant has the right to be compensated for any improvements made during the lease, so leases usually state that the landlord can require the tenant to remove any additions and improvements at its own cost at the end of the lease.

6.4.6 SUBLEASING AND ASSIGNMENT

Under the Tenancy Law, the tenant is entitled to sublet the unit or to assign the lease in the event that the sublease or assignment takes place in the context of a sale or lease of the going concern of the tenant, which the property lease agreement is a part of.

There is no such requirement if the yearly rent exceeds EUR250,000.

6.4.7 TERMINATION

Lease agreements generally provide termination clauses setting out the conditions which, if breached by the tenant, would allow the landlord to regard the lease as terminated.

If the tenant does not hand over the premises once the lease contract expires or it is terminated, the landlord must obtain a court order to recover possession. This can take several months.

6.4.8 SALE OF LEASED PROPERTY

The landlord may transfer the ownership of the leased premises and this does not automatically trigger an early termination of the lease and a clause providing for the termination of the contract in the case of a transfer would be null and void if the Tenancy Act applies.

6.4.9 PRE-EMPTION RIGHTS AND GOODWILL INDEMNITY

If the activity carried out by the tenant involves contact with the general public as users and consumers then:

6.4.9.1 Should the landlord decide to sell the leased premises during the term of the lease or to re-lease it at the expiration of the property lease agreement, the tenant is entitled, as the case may be, to a pre-emption right to purchase the premises or to lease it from the new owner on the same terms and conditions.

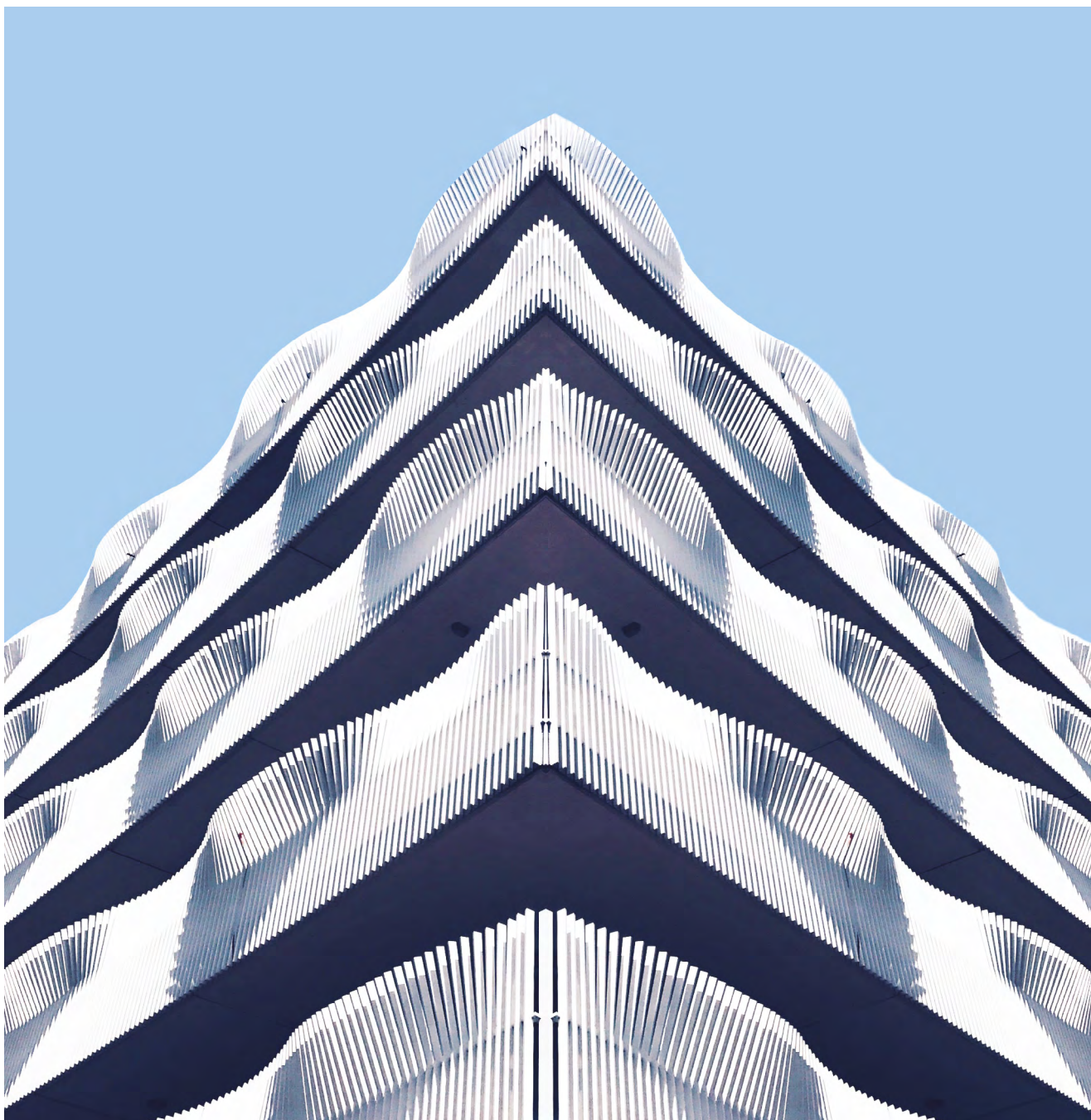
6.4.9.2 Upon termination of the lease (except in certain cases as, for instance, exercise of the withdrawal right, or of the non-renewal right, by the tenant; or termination due to tenant's breach of the contract) the tenant is entitled to be paid an amount equal to 18 times the last monthly rent paid (21 times in the case of a hotel) (a goodwill indemnity).

If the premises are let within a year to a tenant carrying out the same or similar activities, a further indemnity of the same amount is payable to the former tenant.

6.4.9.3 These provisions may be departed from in favor of the landlord if the yearly rent exceeds EUR250,000.

6.5 Public sector tenants

Please be aware that in recent years the Italian government has approved certain specific provisions in favor of public sector tenants (e.g. in relation to rent reductions; rent adjustments; withdrawal rights); therefore in such a case legal assistance by a real estate lawyer would be particularly recommended.



7. Tax

7.1 Taxation on acquisition

The buyer normally pays the transfer tax but both the seller and the buyer are liable for the payment and for any assessment by the tax authorities.

VAT is also paid by the buyer, who can reclaim it by offsetting the VAT due to the tax authorities against its output operations. In some circumstances, a VAT credit can also be obtained.

EU-resident entities may request a refund of VAT paid if certain conditions are met. If the entity is not resident in the EU then it must register for VAT in order to recover any VAT incurred.

7.1.1 RESIDENTIAL REAL ESTATE

Sales of residential real estate are normally exempt from VAT. Residential sales are only subject to VAT if the seller is a construction company that has procured or renovated the property less than five years before the sale takes place, or after five years if the construction company elects in the deed of sale for VAT to be payable. VAT is payable at the rate of 10% (22% if the real estate is registered as a luxury dwelling).

7.1.2 COMMERCIAL REAL ESTATE

The sale of commercial real estate (including offices and industrial property and sales of retail properties and hotel buildings separately from any associated businesses) is subject to VAT at the current rate of 22% (10% in the case of renovated properties) if:

- the seller is a construction company that procured or renovated the property less than five years before the sale; and

- (in any event), if the seller elects in the relevant transfer deed for the VAT regime to apply.

Sales of commercial property, whether or not they are exempt from VAT (except where the seller is an individual), are subject to the following transfer taxes:

- registration tax of EUR200;
- cadastral tax at 1%; and
- mortgage tax at 3%.

Where real estate is acquired by way of shares in the corporate vehicle holding the asset, the transaction is normally VAT exempt. The transfer will, however, be subject to a registration tax of EUR200.

7.1.3 GOING CONCERN

In the case of retail property or hotels, if any licenses or other intangible assets are included in the sale, then the buyer is regarded as purchasing a going concern, since the building is part of a business and the activities on the premises are carried out by means of authorizations held by the owner.

The sale of a going concern is not subject to VAT, although registration tax applies as follows:

- real estate: 9% applied to the net value of the property; and
- other assets (not including receivables): 3% of the net value.

The sale of real estate as a going concern is subject to mortgage tax and cadastral tax payable at a fixed amount of EUR200 each.

7.2 Property Taxes (IMU)

IMU (property tax) is a wealth tax related to the possession of real estate and is calculated on

the basis of the cadastral income (*rendita catastale*) which is set by the competent local tax authority in whose jurisdiction the property is located, on the basis of certain legally established parameters.

Each Municipality is authorized to set the IMU bracket within a range from 0.46% to 1.06%. The IMU due annually is the result of applying the relevant rate within that range to the cadastral value of the property.

As the relevant legislation has been completely amended at least three times in recent years, we strongly recommend engaging professional advice to understand the current status of property taxation.

7.3 Taxation of rental income from real estate – ongoing taxation for the owner of real estate

7.3.1 INVESTMENT VIA AN ITALIAN CORPORATE VEHICLE

If the real estate is leased to tenants, the rental income generated is subject to corporate tax (IRES) at the rate of 24% and regional tax (IRAP) ordinarily levied at the rate of 3.9% although the effective tax rate depends upon the Italian region in which the company is located.

Taxable income for IRES purposes is the net revenue after the deduction of costs, as shown in the annual profit and loss account. With some minor exceptions, all costs relating to the activities of a company can be deducted, including interest (as long as this exceeds interest receivable), up to an amount equal to 30% of EBITDA (not including depreciation and financial lease payments).

20% of the Property tax (IMU) on commercial buildings can be deducted for the purposes of IRES.

10% of IRAP paid and IRAP due on the cost of employees is deductible for IRES purposes.

Depreciation of property is deductible to the extent allowed by law. In certain circumstances, taxable income can be mitigated for IRES purposes by using appropriate leverage. In particular, interest due on loans which are secured by mortgages over real estate for letting is not subject to the 30% threshold and is therefore fully deductible.

The income subject to IRAP is the amount of revenue after the deduction of costs, as shown in the annual profit and loss account. However, not all costs related to the company's activities can be deducted, including interest payments, the cost of employees, IMU and IRES payments.

7.3.2 INVESTMENT VIA AN ITALIAN PARTNERSHIP

An Italian partnership is a transparent entity for tax purposes. Consequently, income deriving from investments is taxed at the level of individual partners, even if this is not distributed as dividends.

Interest is 100% deductible for the purposes of computing the partnership taxable income to be transferred and taxed at the level of the partner (they are not subject to the 30% EBITDA threshold limitation). 10% of IRAP and IRAP due on the cost of employees is deductible from the partnership taxable income.

In the case of non-resident partners, the income is taxed as business income at the level of the partner at the rate of 24%.

Regional tax (IRAP) at the rate of 3.9% applies at the level of the partnership. The income and allowable deductions for the purposes of IRAP are the same as for corporate vehicles.

IMU applies to partnerships in the same way as it does to corporate vehicles.

7.3.3 Investment without a permanent establishment in Italy

In the case of investments without a permanent establishment in Italy (please note that, in contrast to the position in some countries, owning Italian real estate does not automatically give rise to a permanent establishment in Italy), the income derived from letting property is subject to IRES payable at the rate of 24%. 95% of the gross income derived from letting is taxable and no depreciation or other costs can be deducted. Interest on loans secured on the property is not deductible for tax purposes.

Investors without a permanent establishment in Italy are subject to IMU in the same way as Italian entities.

7.4 Taxation on Distributions

7.4.1 INVESTMENT VIA AN ITALIAN CORPORATE VEHICLE

The distribution of dividends to a shareholder in an Italian company is not subject to withholding tax if the shareholder has its registered office in Italy, or if it is a foreign entity with a permanent establishment in Italy. If the shareholding is held by a non-resident entity, withholding tax normally applies at the rate of 26%.

Nevertheless, if the foreign company is resident in another European country, the withholding tax rate is lowered to 1.20%.

Withholding tax may also be reduced by a tax treaty between Italy and the investor's home country.

Provided all the requirements of the EU Parent Subsidiary Directive are met (e.g. a shareholding of at least 10% has been held for at least a year etc.), no withholding tax will be payable.

7.4.2 INVESTMENT VIA AN ITALIAN PARTNERSHIP

In the case of Italian partners, no taxation applies prior to distribution, since the income is taxable at the level of the individual partners under a tax transparency regime, once accrued.

Non-resident partners are subject to tax in Italy on their share of the partnership's worldwide income. Non-resident partners must therefore submit a tax return for corporate or individual income tax purposes. In this case any other income derived from Italy (and not subject to a substitute or final withholding tax) will also be taken into account.

7.4.3 Investment without a permanent establishment in Italy

Once the profits have been taxed in Italy they can be transferred to the foreign parent company without any further taxation.

7.5 Taxation On Disposals

7.5.1 INVESTMENT VIA AN ITALIAN CORPORATE VEHICLE

Profits on the sale of property are subject to IRES, regardless of how much time has elapsed since its acquisition. The profit is the difference between the book value of the property at the time of the sale (as reduced by depreciation) and the agreed purchase price.

In some cases it is possible to spread the liability for tax on capital gains over a period of five years.

Capital gains realized from the sale of property are also generally subject to IRAP at the rate of 3.9%, unless the sale is considered to be an extraordinary activity (i.e. outside the normal activities of the company).

If the property is sold as a going concern (i.e. if it is a real estate asset including licenses and other intangible assets), the sale is not subject to IRAP.

Financial transactions tax (Tobin Tax) is payable by the purchaser of shares in an Italian resident joint stock company, even if the purchaser and the seller are not Italian residents. This tax is levied at a rate of 0.2% on the agreed price. Tobin Tax is not levied on the sale of quotas of a limited liability company.

7.5.2 Direct investment by a foreign company without a permanent establishment in Italy

Capital gains derived from the sale of real estate are not subject to IRES if the property is sold more than five years after its acquisition. If the sale occurs within five years, IRES applies at the rate of 24%. Since depreciation is not permitted in the absence of a permanent establishment, taxable gains comprise the difference between the acquisition cost at the time of purchase and the price agreed for the sale of the property.

7.5.3 INVESTMENT VIA AN ITALIAN PARTNERSHIP

Since an Italian partnership is a transparent entity for tax purposes, any income deriving from the sale of real estate is taxed at the level of the individual partners even if this is not distributed. If the partner is non-resident, income is taxed at partner level at the rate of 24%.

Capital gains are excluded from the IRAP taxable basis of a partnership, unless its normal business activities include the sale of real estate. If this is the case, capital gains would be included in the IRAP taxable basis.

If the property is sold as a going concern (i.e. if it is a real estate asset including licenses and other intangible assets), the sale is not subject to IRAP.

7.6 Real estate funds

7.6.1 TAXATION ON ACQUISITION

Mortgage and cadastral taxes applicable on the acquisition of non-residential buildings are reduced to half when one party to the transaction is a real estate investment fund. This means that mortgage and cadastral taxes on the acquisition of instrumental buildings are applied at the rate of 1.5% and 0.5% respectively.



7.6.2 TAXATION OF RENTAL INCOME FROM REAL ESTATE – ONGOING TAXATION FOR THE OWNER OF A REAL ESTATE

Real estate investment funds are fully exempt from corporate (or individual) income taxes (they are not subject to IRES or IRAP). In other words, rental fees generated by the fund are not subject to taxation in Italy at the level of the fund itself.

IMU is payable by real estate investment funds.

7.6.3 TAXATION ON DISTRIBUTION

Proceeds distributed by a real estate investment fund, whose units are held by Italian institutional investors such as asset management companies or pension funds, or by Italian non-institutional investors owning less than 5%, are subject to a 26% withholding tax distributed by the relevant management company to unit-holders. This is payable as a final withholding tax if the investor is an individual, or as an advance payment of tax if the investor is a corporate entity. Conversely, the mechanism mentioned above is not applied to those real estate investment funds more than 5% of whose units are held by Italian non-qualified investors. Such funds are taxed on the basis of a transparency regime pursuant to which the income generated by the fund is taxed directly vis-à-vis the unit-holders irrespective of the distribution of the income.

As far as non-resident investors are concerned, if the foreign investor is a specific-qualified investor (e.g. funds, pension funds, other sovereign entities) resident in a

white list country, no withholding tax is due on the fund's distributions, otherwise income is subject to a 26% withholding tax, potentially reduced by the applicable tax treaty, regardless the amount of the units held into the Italian real estate investment fund.

7.6.4 TAXATION ON DISPOSALS

Capital gains from the sale of property are included in the fund's net income and taxed at the level of the investors when the income is distributed or upon redemption of the units.

7.6.5 TAXATION ON SALE OF THE UNITS

The potential capital gain realized by foreign investors upon disposal of the units of the fund would be considered as capital gain, for the difference between the sale price and the unit value.

Capital gain realized by an Italian investor upon sale of the units would be subject to:

- 26% substitute tax, in case of investors (i) not holding the units in the ordinary course of their business and (ii) holding a participation in the real estate fund not exceeding 5% of the fund's equity;
- marginal income tax rate (up to 43%) on 58.14% in case of investors (i) not holding the units in the ordinary course of their business and (ii) holding a participation in the real estate fund exceeding 5% of the fund's equity. Starting from January 1, 2019, capital gains realized by such investors would be subject to 26% substitute tax; and

- 24% corporate income tax, if the investor holds the units in the ordinary course of its business activity.

Capital gain realized upon the sale of the units of the fund by a foreign investor would not be subject to taxation, if the investor is resident in a country allowing an exchange of information with Italy or in the case of certain specific institutional investors.

Foreign investors other than those above would be subject to 26% substitute tax, eventually reduced by the provisions included in the double taxation treaty existing and applicable, if any (for instance it may provide that the capital gains realized upon the disposal of participations are taxable only in the country in which the seller is resident).

In case of liquidation or redemption of the units, the difference between the unit value and the acquisition/ subscription value would be considered as proceeds from the fund and taxed accordingly.

7.7 SICAF

7.7.1 TAXATION ON ACQUISITION

Mortgage and cadastral taxes applicable upon the acquisition of not residential buildings are reduced to half when one of the parties to the transaction is a SICAF. This means that mortgage and cadastral taxes upon the acquisition of instrumental buildings are applied at the rate of 1.5% and 0.5% respectively.

7.7.2 TAXATION OF RENTAL INCOME FROM REAL ESTATE – ONGOING TAXATION FOR THE OWNER OF REAL ESTATE

SICAFs are fully exempt from corporate (or individual) income taxes (they are not subject to IRES or IRAP). This means that the following proceeds are not subject to taxation at the level of the SICAF: (i) proceeds deriving from the letting of real estate; (ii) potential capital gain on a sale of real estate; (iii) dividends deriving from any participation in a real estate company held by the SICAF.

IMU also applies to SICAFs.

7.7.3 TAXATION ON DISTRIBUTIONS

Dividends distributed by SICAFs during the investment to foreign investors are not subject to withholding tax upon distribution if received by certain foreign investors (e.g. pension funds and collective investment undertakings established in foreign states or territories included in the white list, compliant with certain requirements provided by the applicable laws).

Dividends distributed by the SICAFs during the investment to foreign investors other than those above, are subject to 26% withholding tax, or to the lower double tax treaty rate where in force and applicable (ordinarily 10% withholding tax).

7.7.4 TAXATION ON DISPOSALS

Capital gains from the sale of real estate by a SICAF are not subject to taxation at the level of the SICAFs and are taxed at the level of the investors.

7.7.5 TAXATION ON EXIT FROM THE INVESTMENT

Italian law provides that gains from the sale of units in SICAFs realized by Italian investors:

- are subject to 26% substitute tax in the case of (i) a participation held in the SICAF lower than 5% of the SICAF net equity and (ii) investors not holding the units in the ordinary course of their business;
- are subject to marginal income tax rate (up to 43%) on 58.14% in case of investors (i) not holding the units in the ordinary

course of their business and (ii) holding a participation in the real estate fund exceeding 5% of the fund's equity. Starting from January 1, 2019, capital gains realized by such investors would be subject to 26% substitute tax; and

- 24% corporate income tax, if the investor holds the units in the ordinary course of its business activity.

Gains from the sale of units in SICAFs realized by foreign investors are not subject to taxation if the investor is resident in a country allowing an exchange of information with Italy (White Listed Countries) or in the case of some specific institutional investors. Otherwise, a 26% substitute tax would be applicable.

The tax regime described above may be affected by the provisions of a relevant double taxation treaty.



8. Real estate finance

8.1 Interest rate risks

Commercial property financing is possible with long-term and short-term loans. In both cases there is a risk of rising interest rates. A decisive counter measure is the selection of fixed interest periods.

However, the risk of interest rate fluctuation still exists at the time of the extension of a loan or upon the conclusion of follow up financing.

This can be hedged against by derivatives, particularly interest rate swaps.

The most common type of interest rate swap is a Plain Vanilla Swap. It is available through the lending institution itself or a third-party financial institution. Within the scope of the Plain Vanilla Swap the borrower agrees to pay a fixed rate to the counterparty, while receiving a floating rate indexed to a reference rate (e.g. three-month Euribor).

With the money received by the counterparty the floating loan interest is paid to the lending institution.

In this way the borrower eliminates the risk of rising interest rates; concurrently the advantage of sinking interest rates is given up and now lies with the counterparty.

8.2 Securities and collateral agreements

As anticipated above, the most common form of security over real estate is a mortgage (*ipoteca*); in the case an investor intends to buy real estate borrowing money from a lender (usually a bank), the lender will normally require a mortgage over the property.

It is also common for the shareholder(s) in a borrower company to grant a pledge (*pegno*) over the shares in the property owning company, and for borrowers to grant:

- a pledge over, inter alia, each bank account held by the borrower itself in relation to the relevant transaction;
- an assignment of the rent receivables;
- an assignment of any other receivables (e.g. construction contracts, sale and purchase agreements, etc.); and
- a loss payee clause an assignment of the receivables deriving from insurance policies relating to the real estate investment).

Under this pledge, the account bank(s) continue to receive instructions relating the operation of the bank accounts from the borrower, until an event of default occurs.

The relevant debtor(s) will continue to pay to the borrower the amounts due to it (until an event of default occurs), but usually such amounts are credited to a bank account pledged in favor of the lender.

The Italian Civil Code allows a creditor (i.e. a lender) to assign its claim against a debtor (i.e. a borrower), provided that the claim does not have a strictly personal character or that the transfer is not forbidden by law.

8.3 Taxation and fees on the creation of security

The following taxes and fees are payable in relation to the granting of security over real estate:

- notaries' fees are payable in fairly substantial amounts in respect of any security document executed as a notarial deed, and such fees vary in proportion to the secured amount;
- nominal stamp duty;
- registration tax: (i) EUR200, if the grantor is securing its own obligations; (ii) 0.5% of the secured amount (or, in relation to shares, the value of the shares, if lower), if securing third parties' obligations;
- mortgage tax is payable at 2% of the secured amount, and
- cadastral tax is payable at 1% of the secured amount.

To avoid paying all of these taxes it is in some cases possible to apply the *imposta sostitutiva* (Substitute Tax). This is an umbrella tax (currently) at a flat rate of 0.25% of the principal amount of the loan from time to time effectively drawn down (Substitute Tax is normally retained by the bank from the advance) but only applies where certain conditions are met and only to particular types of financial transactions, as follows: (i) the loan has a contractual duration of at least 18 months and one day;

(ii) the loan is advanced by EU banks or Italian branches of EU banks, securitization vehicles, insurance companies set up and authorized in a EU Member State or collective investment schemes set up in a EU Member State or in a EES Country included in the white list and (iii) the facility agreement is executed in Italy.

8.4 Lending activity

Italian law reserves the right to carry out lending activities to certain duly authorized entities (i.e. banks and financial intermediaries).

A lending activity is deemed to be carried out vis-à-vis the public when it is carried out (i) on a professional basis and (ii) in respect of third parties.

8.5 Corporate rules

8.5.1 FINANCIAL ASSISTANCE RULES

Financial assistance by an Italian company for the acquisition or the subscription of its own shares is prohibited by section 2358 of the Italian Civil Code, in relation to a joint stock company (SpA), and by section 2474 of the Italian Civil Code, in relation to a limited liability company (Srl).

This prohibition includes all forms of financing, either direct or indirect, any refinancing of existing loans granted for acquisition purposes, and all loans, security or guarantees granted by a company for the benefit of third parties.

The Italian Civil Code does, however, provide that financial assistance to an SpA is possible in some instances subject to the satisfaction of a number of strict requirements.

8.5.2 CORPORATE BENEFIT RULES

To the extent that security or guarantees are provided by a group company, each group company must itself have a specific and economic interest in guaranteeing/securing the financial obligations of its parent company.

As the subsidiary must have an autonomous interest in granting a security, the granting of such security should not have a negative impact on the subsidiary's net worth. This is measured in terms of the potential total payments under any guarantee and/or security not causing the net worth of the Italian grantor to fall below zero (leading to the Italian grantor's insolvency).

The existence of a corporate benefit is a pure business decision and as such it is a matter for the directors to resolve upon. There is no test to certify the existence of a corporate benefit and it should be evaluated on a case-by-case basis.

8.5.3 SHAREHOLDERS' LOAN REPAYMENT

According to section 2467 of the Italian Civil Code, when certain circumstances exist the repayment of a shareholders' loan in favor of the company is subordinated with respect to the repayments of the other creditors and, if executed during the year preceding the bankruptcy declaration, shall be returned to the company.

This provision applies regardless of the form of the funds' injection – when certain circumstances are verified, such as (i) the disparity of the company's indebtedness compared to its net worth or (ii) a financial situation where an equity contribution would have been reasonable.

This provision applies to a limited liability company (Srl) but according to case law it is possible to apply section 2467 also to a joint stock company (SpA) in certain circumstances, in particular when the corporate/business structure of the SpA may be deemed similar to the structure of an Srl (e.g. joint stock companies not having several shareholders and/or a closed corporate structure, or carrying on a small business; but also in the case of loans provided by a controlling shareholder etc.).

According to section 2497 quinquies of the Italian Civil Code, the aforesaid provisions also apply in the case of intercompany loans, with the exception of those granted by a parent company in favor of its subsidiaries.

Glossary

TERM	EQUIVALENT
Piena proprietà	Absolute freehold or full ownership
Diritto di superficie	Right to build
Diritto di usufrutto	Beneficial interest
Diritto d'uso e di abitazione	Right of use
Conservatoria dei Registri Immobiliari	Real Estate Register
Società a responsabilità limitata	Limited liability company – Srl
Società per azioni	Joint stock companies – SpA
Trascrizione	Filing
Diritti reali	<i>In rem</i> rights
Servitù prediali	Easements
Ipoteca	Mortgage
Nuda proprietà	Bare ownership
Diritto di enfiteusi	Emphyteusis
Contratto di locazione	Property lease agreement
Contratto di affitto d'azienda	Business lease agreement
Fondi di investimento immobiliari	Real estate investment funds

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