

Direct Selling

The expert's opinion

Gabriele Labombarda

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Direct selling is a growing sector in Italy: in 2019, it registered an unparalleled 51% growth in terms of quantity of products distributed by the 265 active companies.

Direct selling is increasingly growing also, and mainly thanks to, the important daily activity of the key figures in this market i.e. direct door-to-door salesmen (so-called "incaricati").

The relationship between the company and the salesmen determines the success of a direct selling initiative.

The basic element is a good product, which is recognizable and appealing in the market.

However, the product alone is not enough to achieve success in a network marketing initiative. As the word network suggests...

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Overview

Direct selling: Italian peculiarities

Direct selling is a large and growing sector within the non-store retail trade in Europe. Direct sales volume shows a constant growth over the last years. Italy is one of the top direct selling markets in the world, both by sheer size and growth figures.

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Focus on...

Italian peculiarities: three main aspects

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- a) legal aspects;
- b) tax aspects; and
- c) social contributions aspects.

These aspects affect both the Company and the salesmen...

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Case History

What our clients say about us is the key ingredient of our work. Because thanks to the open confrontation and the transparent exchange of ideas we are able to meet concrete achievements. And so it was for **Adele Pastore - General Manager Italy, Spain, Slovenia of Synergy WorldWide Italy Srl**, who entrusted us with the outsourcing of direct selling related processes...

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Overview

Direct selling: Italian peculiarities

Direct selling is a large and growing sector within the non-store retail trade in Europe. Direct sales volume shows a constant growth over the last years. Italy is one of the top direct selling markets in the world, both by sheer size and growth figures.

There is a clear and stable regulatory environment: with the 2005 law regulating direct selling (Legge 173 dated August 17, 2005) with a special contract for intermediaries, income taxes are levied at source. There is also an income threshold clearly stating the difference between occasional and professional intermediaries and there are severe provisions against pyramid schemes, as well as against ungrounded Health Claims.

Understanding different regulations is important, but understanding the style of communication in each country is important too.

The most successful companies are the ones who actually adapt to the local environment and culture and do their homework before they set up their local operations. The purpose of this memorandum is to provide a short summary to the most relevant provisions which characterize the Italian Direct Selling Market, in particular with regard to the key role played by the Italian “incaricato alla vendita diretta a domicilio”. As a matter of fact, due to the Italian legislation and the benefited schemes it provides, distributors in Italy are not “direct sellers” but are called “demonstrators”, a peculiar kind of intermediary. The Italian term for this is “incaricato”, according to Italian direct selling law. In particular, an Italian incaricato is an intermediary, who is not purchasing a product for re-selling but, on the contrary, he introduces the selling company to a consumer and gains an intermediation commission for the introduction. This system, based on a single sale rather than two sales, makes Italy different from many other countries.

Background

Note that a pure distributive scheme, like the traditional one above, can be legally put in place in Italy. Given no special regimes are set forth for distribution, though, that scheme would significantly affect the net income

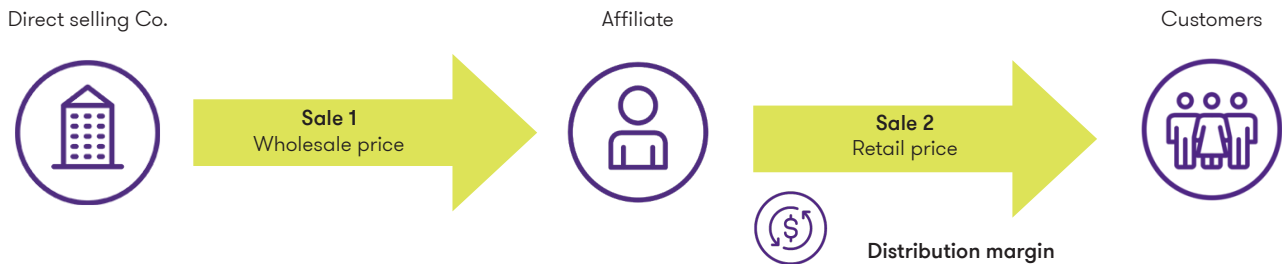
of the distributor, as ordinary taxes (much higher) and personal (expensive) formalities would apply. For this reason, the direct selling industry in Italy is almost entirely working with the Italian benefited scheme for salesmen.



Sales scheme

Traditional direct selling

Income for the affiliate is a distribution margin (e.g. wholesale price is 80\$, Retail price is 100\$: distribution margin is $100\$ - 80\$ = 20\$$).



Italian direct selling

Income for the affiliate is an intermediation fee (e.g. he charges a commission fee of 20\$ for intermediating the sale of a product sold at retail price of 100\$).





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Direct selling is a growing sector in Italy: in 2019, it registered an unparalleled 51% growth in terms of quantity of products distributed by the 265 active companies.

Direct selling is increasingly growing also, and mainly thanks to the, important daily activity of the key figures in this market, i.e. direct door-to-door salesmen (so-called *incaricati*).

The relationship between the company and the salesmen determines the success of a direct selling initiative.

The basic element is a good product, which is recognizable and appealing in the market. However, the product alone is not enough to achieve success in a network marketing initiative. As the word network suggests, there is the need for people to have excellent relationship skills, which are essential to reach exceptional synergies as they are useful both for the company and the product to be distributed, as well as for a better management of an organization made up of salesmen. A good salesman can not only highlight the qualities of a product, but also advise the selling company on how that product can be adapted – or better adapted –



to the reference market, make suggestions on other products to be distributed, on marketing policies to be implemented, etc.

Most of all, a good salesman is able to coordinate in the best possible way the work of a complex organization made up of individuals, who, when duly incentivized according to their personal characteristics and aims, can act in a coordinate way to reach a common objective. When both abilities combine, success is achieved. However, direct selling is also an insidious market, as it is still affected by distrust due to companies that in the past operated through fraudulent mechanism known as pyramid sale schemes.



How to distinguish direct selling from pyramid schemes?

Direct selling is a kind of retail sale activity that is carried out by collecting purchase orders made at the place where the customer is located.

This activity is performed by salesmen, who promote the collection of purchase orders from end customers, whether under an employment contract with the selling company or not. While revenues from direct selling depend on the direct or indirect intermediation of the company's products and services, revenues in pyramid schemes depend on the recruitment of new individuals, who are who are required often to make a high initial investment in order to access the system or to purchase materials, goods, or services. In a pyramidal structure, revenues come from the mere recruitment of other people, without the need to sell goods or services (even though these sales are performed to try and hide the pyramid scheme): this sale scheme is prohibited in Italy pursuant to law n. 173 dated 17 August 2005 concerning direct door-to-door selling activities and the safeguard of consumers from pyramid schemes. The above law provides serious penalties: except for the fact that this would constitute a more serious crime (e.g. fraud), anyone who promotes or realizes or simply takes part in this kind of activities is punished either with detention from six months up to a year, or with a penalty from € 100,000 to € 600,000. Moreover, pyramid schemes are a misleading commercial practice pursuant to art. 23, para. 1, letter p. of the Italian Code of Consumption, for which the Italian Competition Authority (*Autorità Garante della Concorrenza ed il Mercato*) can also inflict fines and/or disqualification provisions.

How to take the best opportunities?

The success of direct selling in Italy is certainly related to the organizational flexibility it provides.

Traditional marketing strategies, characterized by a high competition, are no more effective. Therefore, alternative strategies and new sales channels are needed in order to help companies involving the customer effectively.

For this reason, besides their flexibility and capability to adapt to the context without incurring fixed costs (which are instead required to build a traditional sales network), door-to-door direct selling schemes have registered a considerable success and increasing growth mainly for those companies that were able to use and adapt these systems to their own advantage.

However, there are still uncertainties on the specific relevant regulation and on the interpretations by the Italian Competition Authority and therefore general commercial rules are usually taken as the reference regulation, thus implying some risks.

In this context, the support of an expert and qualified advisor who knows how to build compensation plans and how to lead you through the complex specific tax, social security, and regulatory provisions of this sector is crucial to prevent risks and organize the direct selling activity efficiently and effectively.

At Grant Thornton, we have an over ten-years' experience in this sector and we can assist you with the review of compensation



plans and policies and procedures, with a seamless and integrated management of selling/purchasing cycles, with the maximization of the efficiency of your Group, with the management of the organization according to the sector's best

practices, with regulatory, tax, and procedural compliance (e.g. Privacy, Health Claims, legislative decree no. 231/2011) through specialists that will work in team to ensure our clients an integrated and interdisciplinary approach.

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Case History

Adele Pastore

General manager Italy, Spain, Slovenia Synergy WorldWide Italy S.r.l.

What our clients say about us is the key ingredient of our work. Because thanks to the open confrontation and the transparent exchange of ideas we are able to meet concrete achievements. And so it was for **Adele Pastore – General Manager Italy, Spain, Slovenia of Synergy WorldWide Italy Srl**, who entrusted us with the outsourcing of direct selling related processes.

“The team at Grant Thornton helped us put in place a full automation process for our “galaxy” of salespersons. Since the very beginning, they listened to our needs and together we have built an innovative automated system, which included generation of invoices, automated management of tax and social security calculations, up to final compliance with the new electronic invoicing requirements, that my US colleagues find easy to use too.”

Attention to clients’ needs is often what makes the difference. Our approach is based on the assumption that it is not enough to offer an efficient service, but we want to go beyond and broaden our horizons supporting our clients to arrive where they never thought they could go.

“I love the team proactivity and flexibility in creating tools that are customized to our needs, even anticipating what our needs will be. I know they are now working on another project that I am sure will give us further benefits.”



Focus on...

Italian peculiarities: three main aspects

The peculiar Italian direct selling scheme involves three main aspects:

- a) legal aspects;
- b) tax aspects; and
- c) social contributions aspects.

These aspects affect both the Company and the salesmen.

Legal aspects

1. Definitions - Article 1 of the Italian Law regulating direct selling provides for that:

- with “direct door-to-door sale activity” (hereinafter direct sale) is meant a special kind of retail sale or offer of goods and services, as identified by Article 19 of Legislative Decree no. 114, dated March 31, 1998, that is carried out through the collection of purchase orders at the final consumer’s domicile or in a place where the final consumer stays, also temporary, for personal reasons (i.e. job, study, entertainment etc.);
- with *incaricato alla vendita diretta a domicilio*, i.e. “Person in charge of direct door-to-door sale” - hereinafter also “salesman” or “affiliate” - is meant the person who, with or without a subordinate relationship, promotes, either directly or indirectly, the collection of purchase orders at private consumers’ domicile on behalf of the Company as defined below;

- “Company” refers to the company that carries out the door-to-door direct sale as defined under letter a) above.

2. Accomplishments of the Company which carries out door-to-door direct sale

- Pursuant to Article 19 of Legislative Decree no. 114, dated March 31, 1998:

- the Company that carries out the “door-to-door direct sale” activity, must file a preliminary communication with the Municipality where the company has its registered office;
- the communication under point 1) must indicate: the sector (e.g. food, food supplements, cosmetics, or other) the Company operates in, the specific professional requirements met by the legal representative of the Company, if and to what extent the Company sells food;
- operations can start after thirty days from the receipt of the communication under point 1) by the Municipality (SCIA);
- the Company which intends to carry out the direct sale through salesmen must communicate the list of the salesmen to the Public Security Authorities of the Company’s jurisdiction;
- the Company is liable for the activity of the salesmen for civil purposes;
- the salesmen must provide evidence that specific requirements are met (i.e. they should have not been sentenced for crimes);
- the Company must provide the salesmen with a personal badge. Should the requirements under point 6) no longer exist, the badge should be withdrawn by the



Company;

- the badge under point 7) must be numbered and updated each year and should indicate the salesman personal data, i.e. name and address, as well as his/her picture;
- the aforementioned badge must clearly indicate the company's registered office, its products, the name of the legal representative as well as his/her signature;
- the badge must be displayed during sales operations.

3. Relationships between the Company and the salesmen - Sales intermediation can be carried out through:

- subordinate employment contracts, between salesmen and the Company. In this case the Italian standard rules governing employment relationships will apply;
- agency contracts, between salesmen who perform this activity customarily and the Company. In this case the Italian standard rules governing Agents will apply;
- salesmen who promote, directly or indirectly, the collection of purchase orders customarily (above the € 5,000 threshold of the salesmen's annual income) or occasionally (under the € 5,000 threshold of the salesmen's annual income). From a tax and social security contribution point of view, salesmen (occasional and habitual) are subject to specific regimes outlined in paragraph below.

We would like to point out that the accomplishment under paragraph 2 must

be fulfilled by the Company regardless of the kind of relationship existing between the salesmen and the Company.

4. . Formalities to be respected for engaging a salesman - A written form is mandatory for engaging a salesman. The engagement can be terminated by the salesman at any time without any further obligations. The written engagement must indicate the following rights and obligations:

- no further obligations shall be respected by the salesman when terminating his/her engagement except for a written communication to be sent to the company by registered letter with return receipt;
- when terminating his/her engagement, the salesman is obliged to return any demonstration goods and materials provided by the Company;
- should the salesman return the demonstration products and material within thirty days, the Company shall refund any amounts eventually paid by the salesman. The refund is subordinated to the integrity of the goods and materials returned;
- the Law restriction reported in paragraph 5 below;
- the terms and conditions of sale, established by the Company, the salesman must comply with;
- unless otherwise expressly provided for in writing, the salesman does not have the authority to collect any consideration or to grant any reductions in price or delays of payment to the private consumers;



- the compensation of the salesman consists in the commissions on the transactions that are accepted and regularly executed;
- the commissions fees and the terms of payment.

Failure to comply with the requested formalities implies the application of administrative penalties (see paragraph 6).

5. Law restriction - The Italian Law provides for that the Company cannot oblige the salesman to:

- a) purchase materials traded or distributed by the Company except for those demonstration goods and materials necessary to carry on its activity that can be compared to a collection of samples;
- b) purchase services, directly or indirectly, from the Company, that are not closely inherent and necessary to the business activity carried out, and however, not proportionate to the volume of the activity carried out.

Unless otherwise expressly provided for in writing, a salesman does not have either the authority to collect the consideration of the purchase orders from private consumers, or to grant reductions in price or delays of payment.

The compensation of the salesman without subordination consists in the commissions on the transactions accepted and regularly executed. The commission fees and relevant terms and conditions must be set down in writing. Other restrictions to be taken into account concerning salesmen are provided for by the Law. Article 5 of Law no. 173/2005 that

clearly states that both the promotion and the realization of activities and structures of sale are prohibited if the primary economic incentive of the salesman is based on the recruitment of new subjects (salesmen) rather than on their actual ability to sell or to promote goods or services directly or through other members.

The promotion of schemes which link the possibility of gain with the recruitment of other persons and in which the right to recruit could be transferred by the mere payment of a consideration is also prohibited as illegal.

6. Penalties - Except for the fact that this would constitute a more serious crime, anyone who promotes or realizes activities or selling structures regarded as pyramidal or encourages the operations under paragraph 3.1.5., is punished either with detention from six months up to a year, or with a penalty from € 100,000 to € 600,000.

Failure to comply with the formalities reported under the paragraph 3.1.4 imply the application of administrative penalty from € 1,500 to 5,000.

Tax and social security contributions aspects

Assumptions

The main element that has to be carefully evaluated, in order to apply the appropriate tax and contributions regime for salesmen, is provided for by Art. 3 of Law no. 173, dated August 17, 2005.

The aforementioned rule clearly states that the activity carried out by a salesman is qualified



as occasional if, and to the extent that, the net income obtained from such activity does not exceed € 5,000 per year.

Considering the above, in order to apply the right regimes both from a tax (direct and indirect) and social security contributions point of view, salesmen under the net income threshold of € 5,000 must be distinguished from the others.

In this respect, please note that a salesman reaches the net income threshold of € 5,000 whenever he/she collects an amount of commission equal to € 6,410 (gross).

As a matter of facts, according to Article 25-bis of Presidential Decree no. 600/1972, the salesman's income is calculated by applying a 22% deduction on the commissions received.

Therefore, a salesman shall be considered:

- occasional: if the income is below the threshold of € 5,000 (equal to an amount of commissions received not exceeding € 6,410);
- habitual: if the income is above the € 5,000 threshold (equal to an amount of commissions received exceeding € 6,410).

Occasional salesman

Direct Taxes: the commissions received by the salesman are not cumulated with other possible income collected during the FY. Furthermore, the commissions received shall not be declared in the salesman's income tax return. The commissions the salesman receives against the direct selling activity are subject to a substitutive tax withheld at source,

applied at 23% on 78% of the commissions (the salesmen) received, according to the provision of Art. 25-Bis of Presidential Decree no. 600, dated September 29, 1973 .

The Company, as a withholding agent, is in charge of the application of the withholding tax to the salesmen and of the payment of the amount withheld to the Italian tax Authorities, on behalf of the salesmen, so that the latter receives a commission fee net of taxes.

Indirect taxes - VAT: occasional salesmen are not considered as VAT taxpayers and they are not obliged to apply for a VAT position.

When the door-to-door sale activity is carried out occasionally by the salesman, it can be carried out without any VAT registration.

The above means that, below the € 5,000 net income threshold per year, no VAT on commissions is applicable.

Exceeding the threshold obliges the salesman to register for VAT purposes.

Once the salesman registers for VAT, he will remain a VAT taxpayer for all following years, hence his/her commissions will always be subject to VAT (at the ordinary 22% VAT rate).

Social security contributions: Social security contributions are not due by salesmen whose annual income does not exceed the threshold of € 5,000. In particular, Art. 44 of Law Decree no. 269, dated September 30, 2003, clarifies that door-to-door direct salesmen have to pay social security contributions only in case the annual income deriving from said activity exceeds € 5,000.

Differently to VAT, the threshold above applies



on a yearly recurring basis. This means that every year the first € 5,000 of net commissions are free of social security contributions.

Habitual salesman

Direct Taxes: also in case of habitual salesmen, the commissions received are not cumulated with other income.

In this case too, commissions received by the salesman shall not be declared in the annual income tax return. As per occasional salesmen, according to the provision of Art. 25-Bis of Presidential Decree no. 600, dated September 29, 1973, commissions received from habitual salesmen for the activity of direct selling are subject to a substitutive source-withholding tax, applied at a 23% rate on 78% of the commissions received (by the salesmen). Even in this case, the Company as a withholding agent is in charge of the application of the withholding tax to the salesmen and of the payment of the amount withheld to the Italian tax Authorities.

Indirect taxes - VAT: the salesman's activity, when it exceeds the € 5,000 net income threshold (i.e. when the commissions received exceed € 6,410), becomes relevant for VAT purposes. The salesman becomes a VAT taxpayer from the first operation that implies

that the € 5,000 net income threshold is overcome. At this time, the salesman must register for VAT according to Art. 35 of the Presidential Decree no. 633, dated October 26, 1972 (Italian VAT Law), and has to comply with the obligations set forth by the Italian VAT Law.

Social security contributions: once the income threshold of € 5,000 is exceeded, also social security contributions are due by the salesman.

According to Art. 44, Law Decree no. 269/2003, salesmen whose annual income exceeds the threshold of € 5,000, must register to INPS Separate Management, starting from the first operation implying that the € 5,000 net income threshold is overcome.

Differently to VAT, the threshold above applies on a yearly recurring basis. This means that every year the first € 5,000 of net commissions are free of social security contributions. Starting from 1st January 2018, social security contributions are due at a 33.72% rate for person which is not registered for any other social contribution duty, 24% for person subject to other social contribution dues (e.g. employees, retired, etc).

Social contributions, calculated by applying 33,72% on the salesman's income exceeding the threshold of € 5,000 net, are borne as follows:



- for 1/3rd by the salesman;
- for 2/3^{rds} by the Company.

No contribution is calculated on yearly income higher than € 103,055 (i.e. Social Security Contributions Cap).

The Company is in charge of withholding 1/3rd of the total contribution due from the salesman and of paying the total amount of the contribution due (i.e. 1/3rd + 2/3^{rds}) to INPS in its quality of withholding agent.

The salesman is in charge of his/her own registration with INPS.

Conclusions

Considering the Italian strict provisions regarding salesmen and the relevant direct selling activity, should the Company decide to carry out this business in Italy, we would recommend incorporating a subsidiary in Italy.

As explained above, a Company that carries out a direct selling activity in Italy through salesmen has to:

- file the relevant communication with the Municipality in which it has its legal office;
- file a communication with the Social Security Institution in the town/area where it has its legal office, for each salesman

engaged;

- supply salesmen with their personal badge;
- engage salesmen in a written form;
- act as a withholding agent for taxes and contributions purposes, applying all relevant formalities briefly described in this document.

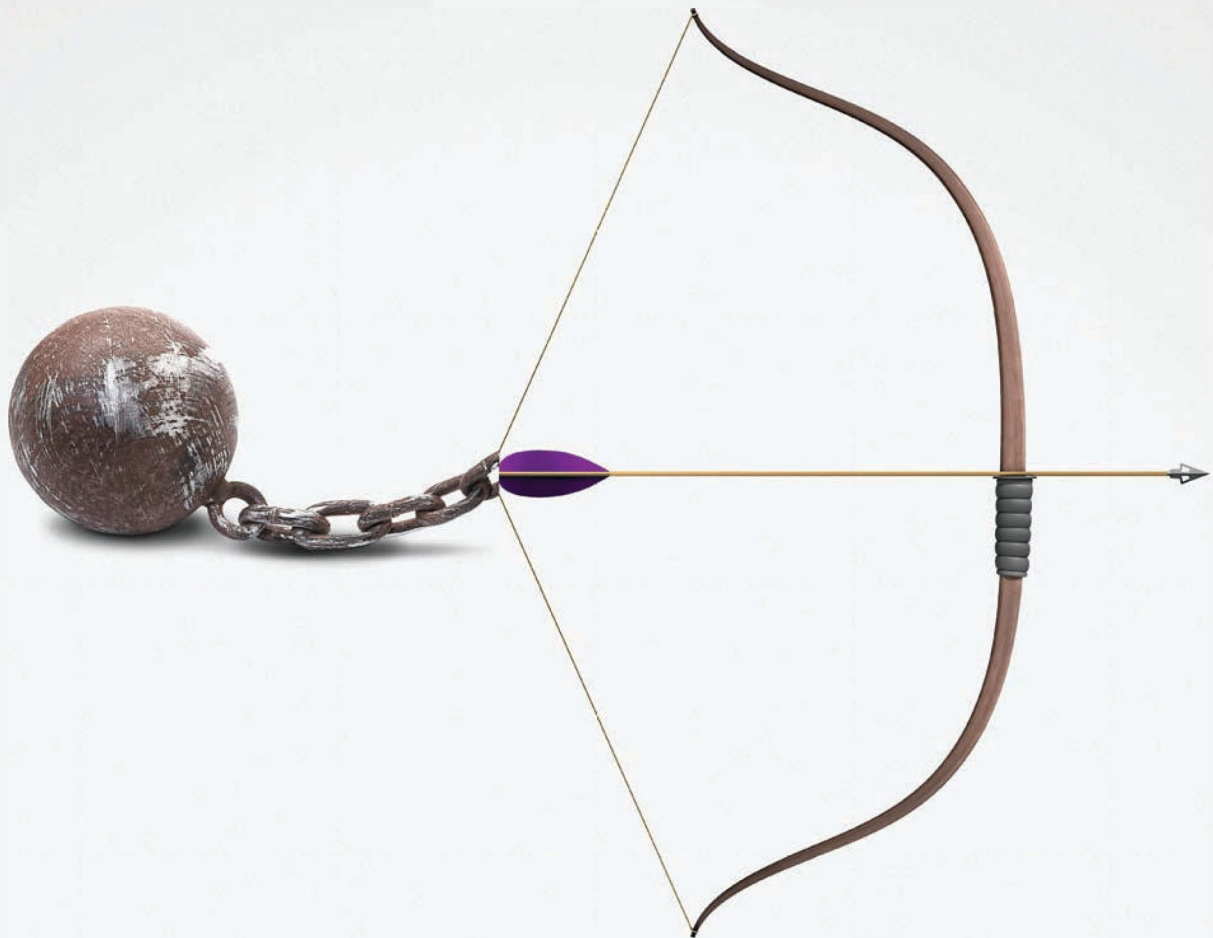
Furthermore, it should:

- ensure its compensation plan and policies and Procedures are compatible with local requirements and interpretations (to prevent significant issues like application of non-compliance penalties or disqualification sanctions by the Antitrust Authority);
- comply with EU regulations (e.g. on the use of Health Claims, GDPR – General Data Protection Regulation, HACCP – Hazard Analysis Critical Control Point, etc.).

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