

Tax Opportunities for Enterprises Investing in Italy

The Italian legislation provides for several tax incentives mostly aimed at promoting investments. The main measures are directed to companies and individuals carrying on the business of an enterprise in the territory of the State and include: Patent Box Regime; Allowance for corporate equity; Research & Development tax credit; Super-amortization and Extra-Amortization; VAT grouping rules.

In addition, a special New Residents regime for individuals moving to Italy has been introduced.

Furthermore, recent initiatives have been taken in order to promote the dialogue between taxpayers and the Italian Revenue Agency, and to ensure certainty and compliance in tax law. In particular:

- the General Taxpayer's Advance Ruling and the Advance Tax Agreements for enterprises with international activities have been enhanced;
- the Cooperative Compliance Program and the Advance Tax Ruling on new investments have been introduced.

Tax incentives

A. Patent box.

Aim. The Patent Box regime is a tax bonus introduced to improve exploitation and development of intellectual properties (IPs) deriving from research and development activities, in order to increase enterprises' competitiveness and growth.

Benefits. The incentive entails an optional partial tax exemption (up to 50%) from corporate tax for income deriving from the direct exploitation of intellectual property (for instance, profits deriving from sale or use of the IP, net of relating expenditures) or from licensing of the IP (such as

royalties earned by the taxpayer, net of all IP-relating costs). In order to determine the benefit, we had adopted the so called “modified nexus approach”: this means that there must be a direct nexus between R&D activities and qualified IP, as well as a direct nexus between qualified IP and qualified income. The Patent Box regime requires taxpayers to submit to the Italian Revenue Agency a query for an ad hoc tax ruling, leading to a binding agreement between the Italian Revenue Agency and the taxpayer. This agreement is aimed at determining the methods to be followed in order to define the income deriving from the direct exploitation of IPs.

Qualifying persons. The benefit is granted to taxpayers carrying out research and development activities related to IPs (companies; individual entrepreneurs; other entities, different from companies, carrying on business activities). Also non-resident taxpayers with a Permanent Establishment in Italy may benefit from the Patent Box if they are resident in a country with which Italy has an effective tax information exchange agreement in force.

Qualifying assets. Eligible intangible assets are software protected by copyright, patents, trademarks including collective brands, business and technical-industrial know how, other legally protected IP (such as designs and models).

B. Allowance for Corporate Equity (ACE, also known as Notional Interest Deduction - NID).

Aim. The tax incentive has been introduced to promote the recapitalization of undertakings and to mitigate the different tax treatment applied to companies funded with debt compared to that applied to companies funded with equity.

Benefits. ACE benefit entails a notional deduction from corporate income taxable base. The deduction corresponds to the net increase in the

“new equity” employed in the entity (meaning the equity generated after 2010), multiplied by a rate which is fixed at 2.3% for FY 2017 and increased at 2.7% for FY 2018 and thereafter.

Qualifying persons. The incentive shall be granted to:

- resident companies;
- individual resident entrepreneurs;
- resident partnerships;
- other commercial resident entities;
- Permanent Establishments in Italy of non-resident companies.

Qualifying increases. The eligible equity increases may be inclusive of equity contributions and retained earnings.

C. Research & Development tax credit.

Aim. The aim of the benefit is to encourage investments realized by taxpayers in R&D activities.

Benefits. The incentive leads to the recognition by the Revenue Agency of a tax credit up to 50% of the increase of annual R&D expenses as compared to the historical average of the same expenses incurred during FYs 2012, 2013, 2014. The tax credit is neither included in the income tax base nor in the regional tax on productive activities base. Therefore, taxpayers are entitled to use tax credit in the payment form in order to reduce the amount of income or regional taxes, as well as VAT and social security contributions.

Qualifying persons. The bonus is available to any enterprise (irrespective of its legal form, business sector, accounting standards and size) and also to Italian undertakings or Permanent Establishments in Italy of non-resident taxpayers, performing R&D activities on the basis of agreements entered into with non-Italian companies resident in EU States,

or in a European Economic Area (EEA) countries or other country partners with which an exchange of information instrument is in force.

Qualifying expenses. The right to benefit is granted to these entities once proved that they invest in the qualifying R&D activities such as fundamental research, industrial research and experimental development. They have to spend at least 30,000 euros per year, while the maximum yearly credit for each beneficiary is established at 20 million euros. To see the benefits applied, taxpayers have to support R&D qualifying costs between 2015 and 2020. The eligible expenses are:

- costs connected with workers employed in the above-mentioned R&D activities;
- depreciation charges related to the assets employed to carry on the activities/projects;
- R&D extra-muros activities bought on the base of a contract signed with universities, other research institutes and equivalent bodies and other enterprises;
- technical expertise, industrial and biotechnological patents.

R&D tax credit is a general measure; taxpayers can benefit of R&D tax credit jointly with other incentives, unless the rules of these incentives are otherwise stated . In any case, the sum of the tax credit and the other incentives, relating to the same eligible expenses, cannot exceed the said eligible costs.

D. Super-amortization and Extra-amortization.

Aim. These provisions facilitate business investments by allowing an extra-amortization on the purchase of certain tangible assets, in order to stimulate the renewal of capital goods.

Benefits. The fiscal amortization charges in relation to purchases of new capital goods will increase their value by 40% or 150% with respect to their book value, for the whole amortization period.

Qualifying persons. Enterprises of any type are entitled to benefit of the increased fiscal amortization charges. The benefits are also granted to Permanent Establishments in Italy of non-resident investors.

Qualifying purchases: The increased amortization charge fixed at 40% (super-amortization) is applicable in relation to purchases realized from 15 October 2015 to 31 December 2017. The purchase period is extended up to 30 June 2018, on condition that purchase orders have been accepted by the seller by 31 December 2017 and that at least 20% of their price has been paid by the same date. The amortization charges are increased up to 150% of their value (Extra-amortization) for some listed “smart equipment” which is allowed to benefit from specific digital and technological transformation processes under the model promoted by the Italian Government plan for industrial growth named “Industry 4.0 Plan.” Another additional 40% super-amortization is also introduced for certain intangible assets such as software, IT systems and platforms related to the above mentioned “Industry 4.0 Plan”.

E. VAT grouping rules

Aim. In order to simplify the application of VAT rules for company groups and to reduce fiscal burdens, special VAT grouping rules have been introduced, running from FY 2018.

Benefits. As a consequence of the application of this regime, the group itself will be considered as a single VAT taxable person. Therefore:

- transactions carried out between the companies of the group will not be subject to VAT;
- transactions carried out between a group member and a third party will be treated as being made by the group as an entity.

Qualifying persons. The option is reserved to companies closely bound by the following financial, economic and organizational links:

- they have to be subject to a common control, through a direct or indirect participation granting 50% or more of voting rights; this requirement is satisfied even if the common controlling party is based in a foreign Country with which an exchange of information instrument is in force with Italy (i.e. financial link);
- they must perform the same core business and economic activities, or, alternatively, the activities must be complementary, ancillary and auxiliary with respect to the other group members (i.e. economic link);
- a coordination between the decision making bodies of the involved entities has to exist (i.e. organizational link).

Once the election for this regime is made, all entities fulfilling the requirements must adhere to the group (i.e. All-in/All-out)

F. New Residents regime.

Aim. The tax bonus seeks to enhance investments by attracting to Italy high-net-worth individuals with relevant spending capacity.

Benefits. High-net-worth individuals transferring their tax residence to Italy are enabled to apply a substitute tax to their foreign income and gains, amounting to €100,000 for each fiscal year, in lieu of the Italian Income Tax. Therefore, this taxation represents an alternative to the application of the ordinary taxation and the option is valid for a period of 15 years. The election for the regime may be extended to family members through the payment of a substitute tax amounting to €25,000 per member, on their foreign income and gains. In order to benefit from the regime, all applicants have to submit a preliminary ruling to the Italian Revenue Agency in order to prove the existence of the eligibility requirements. Individuals transferring their tax residence have to pay

inheritance and donation tax only for properties and assets existing within the Italian territory.

Qualifying persons. This favourable tax regime is available for “newly resident” individuals in Italy, who (regardless of their nationality or domicile) have been non-tax resident in Italy for at least 9 years out of the 10 years preceding their transfer to Italy. The incentive regime may be also extended to the family members of these individuals.

Tax compliance instruments

A. Cooperative Compliance program.

Aim. The regime, initially launched in 2013 as a pilot project, has been introduced in Italy in order to promote an enhanced and closer cooperation with the Italian Revenue Agency.

Benefits. Taxpayers are allowed to enter into advance discussions with the Italian Revenue Agency in order to reach a common evaluation of potential tax risks before the filing of tax returns and to assure tax certainty. Furthermore, admission to the Cooperative Compliance regime allows taxpayers to benefit from several advantages:

- a fast track ruling (no more than 45 days since the receipt of request or the integration of documents) regarding the application of tax provisions;
- tax penalties are reduced of 50% and, in any case, applied to an amount not exceeding the minimum provided by law;
- obligation to provide guarantees is not envisaged for taxpayers intending to obtain tax refunds.

Qualifying persons. The regime is addressed to large taxpayers fulfilling the following requirements:

- resident and non-resident entities having a permanent establishment in Italy with a total turnover or operating revenues exceeding 10 billion euros;
- resident and non-resident entities having a permanent establishment in Italy with a total turnover or operating revenues equal to at least 1 billion euros, which applied for the pilot project launched in 2013;
- entities granting execution to the opinion of the Italian Revenue Agency in response to the Advance Tax Ruling on new investments, notwithstanding threshold of turnover or revenues.

In addition, the access to the Cooperative Compliance program can be extended to resident and non-resident entities having a permanent establishment in Italy, performing strategic direction functions in relation to the tax control framework, regardless of the amount of turnover or revenues.

In order to adhere to the program, eligible taxpayers must file an application including fundamental information on the enterprise, with particular regard to the adopted tax control framework for detecting, measuring, and managing the tax risk.

B. Advance Tax Agreements for enterprises with international activities.

Aim. Advance Tax agreements are binding agreements (replacing the former “international standard rulings”) aimed at promoting the internationalization of companies by giving certainty to the definition of calculation methods and the assessment of factual elements, that can be challenged by the Italian Revenue Agency.

Benefits. These agreements can be concluded by enterprises with international activities wishing to reach a prior settlement and a shared evaluation with the Italian Revenue Agency about:

- the determination of the arm's-length price of transactions between an Italian company and a non-resident company belonging to the same group;
- the definition of entry and exit value of assets in case of transfer of residence;
- the prior assessment on the existence of a permanent establishment in the territory of the State;
- the application to a specific case of rules, including international treaty rules, concerning the payment to (or the receipt from) non-resident companies of dividends, interests, royalties or other income;
- the application to a specific case of rules, including international treaty rules, in order to define the amount of income attributable to a permanent establishment in Italy of a non-resident company or to a permanent establishment in foreign countries of an Italian resident company.

Also “Patent Box” regulatory regime is covered by the Advance Tax Agreements procedure.

Qualifying persons. The status of “enterprise with international activity” is recognized to resident enterprises which (alternately or jointly):

- make transactions with non-resident companies belonging to the same group;
- either hold stakes in the assets, funds, capital of non-resident persons or have stakes in their assets, funds, capital which are held by non-resident persons;

- have paid out to or received from non-resident persons dividends, interests or royalties;
- conduct business through a permanent establishment in another country;
- transfer their residence from Italy to another State or from another State to Italy.

The status of enterprise with international activity is also recognized to non-resident enterprises conducting or intending to conduct their own activity in Italy through a permanent establishment.

C. General Taxpayer's Advance Ruling.

Aim. The aim of Taxpayer's Advance Ruling, provided by Taxpayers' Bill of Rights, is to give taxpayers the possibility to obtain a preventive and written opinion by the Italian Revenue Agency providing the correct application of specific tax provisions. The Taxpayer's Advance Ruling can be considered as one of the "tax compliance institutes" since its preventive nature allows taxpayers to orient their behaviour and, consequently, to prevent litigations with the Revenue Agency. In other words, taxpayers can manage their tax risks under the principle of fair cooperation with Revenue Agency.

Benefits. The Revenue Agency's reply has to be given within certain deadlines laid down by law, and if the Agency does not issue the response respecting the time limits, the taxpayer's interpretation (where represented in the query) is deemed to be accepted (i.e. "silence means assent" rule). With respect to issues covered by the reply, all administrative acts adopted by Tax Authorities in contravention of the same reply shall be null and void (including the interpretation on which "silence means assent" was adopted). It follows that the reply prevents auditors from expressing objections not in line with it (as long as there are no changes in the legal and material conditions on the basis of which the reply was given).

Qualifying persons. Both resident and non-resident taxpayers (directly or by means of their elective representatives in Italy) are entitled to forward the query to the Italian Revenue Agency. The query has to be submitted before the application of the tax provisions.

Types of rulings. The Taxpayers' Bill of Rights provides four types of Advance Tax rulings:

- ordinary rulings: where there is objective uncertainty as to the correct interpretation of a provision (i.e. interpretative ordinary ruling) or where the objective uncertainty is related to the legal and fiscal qualification of a specific case (i.e. qualifying ordinary ruling).
- probatory ruling: where the request is related to the fulfilment of the conditions and to the assessment of the probatory elements required for the adoption of specific tax regimes, in cases expressly provided by law;
- anti-abuse ruling: if the query pertains to the application of the “abuse of right” principle to a specific case, aiming at verifying if a transaction may be considered as abusive;
- anti-avoidance ruling, if the request is aimed at the disapplication of tax provisions limiting (in order to fight avoidance) deductions, tax benefits, tax credits or other subjective positions of the taxpayer; this ruling constitutes the only case in which the taxpayer is obliged to refer to the Tax Authority.

D. Advance Tax Ruling on new investments.

Aim. The Advance Tax Ruling on new investments pursues the main aim to give more certainty to economic operators in the determination of fiscal burdens connected to the implementation in Italy of relevant and qualified business plans.

Benefits. By presenting a single query, investors can obtain from the Italian Revenue Agency an opinion concerning any kind of tax issues (even cumulatively) with respect to a specific investment plan (e.g., tax treatment of leveraged buy-out transactions and application of international treaty rules to incomes deriving from the investment in Italy, such as dividends, interests, royalties or others).

The Advance Tax Ruling on new investments is characterized by a special “vis attractiva”, which entails that the applicant who has already submitted a first ruling on new investments, is entitled to present, in a second time, further questions concerning other operations related to the whole investment plan, regardless of their specific amount.

The Italian Revenue Agency cannot amend the reply to the application. The opinion shall be binding for the mentioned Agency with respect to the investment plan as described by the applicant and valid until the conditions of law and fact, on the basis of which it was given, remain unchanged. Regarding issues covered by the reply, any administrative act (even if containing impositions or penalties) emitted by any Tax Authorities in violation of the same reply shall be null and void. The exercise of the ordinary powers of supervision remains for the competent Tax Authority structures (other than Revenue Agency) only if regarding issues different from those covered by the reply.

Qualifying persons. Persons eligible to file the ruling are:

- corporations and other resident entities running business activities, even if controlled by non-resident entities;
- non-resident companies and institutions of all kinds, regardless of whether they have a permanent establishment in the State or not;
- individuals or persons not running business activities, as long as they are looking to carry out a business activity in Italy or to participate in the equity of a pre-existing enterprise. For instance,

banking foundations may submit the application for the Advance Tax Ruling on new investments, as well as collective investment undertakings (CIUs) – both considered in Italy as non-commercial entities.

Qualifying investments. The procedure enables investors going to realize relevant investments (at least €30 million) within the Italian territory, with significant and long-lasting impacts on employment levels (increase or maintenance).

Conclusion

Based on above mentioned tax opportunities, Italy has launched a new deal of the relationship between Revenue Agency and taxpayers, based on dialogue and cooperation, and aimed at reducing tax uncertainty in planning investments in Italy. In fact, during FY 2016, the Italian Revenue Agency:

- signed the first Cooperative Compliance agreement with a large Italian company;
- concluded several Advance Tax Agreements concerning Patent Box regime;
- answered to several Advance Tax Rulings on new investments.

The combination of tax compliance instruments and tax bonus enables foreign investors intending to promote new economic activities within the Italian territory to benefit of higher levels of legal certainty and lower levels of taxation.

As an example, a non-resident investor willing to realize investments in Italy may incorporate a new company (hereinafter, newco) through injections of new equity, in this way creating the conditions to apply ACE regime.

If this newco runs a business activity or establishes an operating company in R&D fields, it may have access to R&D tax credit and if its activity generates new IP, the newco may also be entitled to benefit of Patent Box regime.

In order to clarify the tax treatment of the whole operation, an Advance Tax Ruling on new investments may be submitted.

If the entities involved in the investment are intending to grant execution to the opinion of the Italian Revenue Agency in response to the Advance Tax Ruling on new investments, notwithstanding threshold of turnover or revenues, they may have access to Cooperative Compliance program.

Where transactions with related parties take place in the investments, it is also possible to achieve the signing of a binding Advance Tax Agreement to determine, for instance the arm's-length price of transactions or the application of rules, including international treaty rules, concerning, for instance, the receipt of dividends, interests, royalties or other income.

Moreover, the incorporation of an operating company by the newco enables these two Italian companies, controlled by the non-resident person establishing the newco to realize the investment, to adhere to VAT grouping rules (starting from 2018).

Finally, managers and individual shareholders participating in the newco (and their relatives) may have convenience in transferring their residence to Italy and in paying the substitute tax under the New Residents regime.