Italia issues significant tax measures including new step-up opportunities and provisions for Digital Economy companies

This Alert highlights the most significant Italian year-end tax changes introduced by the 2014 budget law (2014 Stability law), Law Decree no. 145/2013 (Destination Italy Decree)¹ and other measures.²

As a consequence of the new rules, groups with Italian operations should carefully review the impact of each of the new provisions in order to identify opportunities, manage any risks and comply with any documentation requirements associated with the addressed measures.

One-off asset step up to be taken in the 2013 balance sheet

The 2014 Stability Law introduced a one-off opportunity for Italian companies to step up certain assets reported on the statutory accounts balance sheet related to the fiscal year ending on 31 December 2013 (or after for companies which do not have a calendar year). To the extent the tax basis is less than the book carrying value prior to the election, companies are also permitted to make a step-up only for tax purposes equal to the difference between the book carrying value and tax basis prior to the election (Tax Realignment). Italian companies reporting under International Accounting Standards (IAS) are only eligible to make the election for the Tax Realignment. Among other things, this regime requires the payment of a 16% substitute tax in exchange for a higher tax base to be depreciated/amortized at approximately 31.4%.

One-off opportunity for nonresident companies to step up Italian participations

The 2014 Stability Law re-vamps a special one-off opportunity for nonresident entities to elect for a tax step up of participations in unlisted Italian companies held at least from 1 January 2014, through the payment of a 2% or 4% substitute tax.
 Generally, this provision may be of specific interest to foreign entities not eligible for treaty protection.

**Step up of intangibles related to consolidated subsidiaries**

The 2014 Stability Law reintroduces and makes permanent a rule which allows Italian companies to step up intangibles (including goodwill) related to resident and nonresident controlled companies if included in the Italian statutory consolidated balance sheet. The election implies the upfront payment of a 16% substitute tax in order to benefit from tax amortization at a higher rate of at least 31.4%.

**Increase of the notional interest deduction for 2014 through 2016**

The 2014 Stability Law sets out the notional interest deduction (NID) rates for 2014, 2015 and 2016 at 4%, 4.5% and 4.75% respectively.

**Special provisions for Digital Economy companies**

The 2014 Stability Law provides that entities involved in the collection of on-line advertisement and in related auxiliary services on behalf of foreign group companies must use profit level indicators other than those applicable to the costs incurred in the conduct of their business unless they reach an APA with the tax authorities.

From a VAT perspective, starting from 1 July 2014, advertising services and sponsored links purchased on-line as well as certain on-line advertising services must be purchased exclusively from entities holding an Italian VAT registration. The enacted provision is not fully clear and appears questionable from a European Law perspective.

**International Standard Ruling**

The Destination Italy Decree introduces significant changes to the International Standard Ruling procedure by extending its scope to preliminary assessments of Italian permanent establishments of nonresident entities. The legal validity of the ruling is extended from three to five tax years.

**Deferred Tax Assets monetization regime extended to IRAP**

The 2014 Stability Law makes the Deferred Tax Assets (DTAs) monetization regime, currently applicable only for corporate income tax (IRES), also applicable to the Regional Tax on Productive Activities (IRAP).

**Applicability of transfer pricing adjustments for IRAP purposes**

The 2014 Stability Law provides clarifications on the application of the transfer pricing rules to the determination of the IRAP base.

Other important tax measures relate to:

- IRAP deductions for new employee costs.
- Important simplifications on the tax treatment of bad debt losses and receivable write-downs also for banks and insurance companies.
- New deduction rules for lease fees.
- R&D tax credits for the period 2014-2016.
- Major changes to the substitute tax regime for medium and long term financings.
- Tax surcharge for banks and insurance companies for FY 2013.
- Increase of lump-sum registration tax from €168 to €200.
- Changes to real estate transfer taxes.
- Introduction of a required certification for tax return credits exceeding €15,000.
- Increase of annual tax credit compensation threshold from €516,000 to €700,000.

**Endnotes**

1. The decree was published in the *Official Gazette* no. 300 of 23 December 2013 and entered into force on 24 December 2013. The Parliament has sixty days to convert it into an ordinary law.

2. For additional details, see EY Tax Alerts, *Italy issues new laws with important transfer pricing and VAT implications*, dated 3 January 2014 and *Italy issues 2014 budget law and other significant year-end tax measures*, dated 10 January 2014.
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