

Italy's 2021 Budget Law: A review of key tax measures

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Executive summary

The Italian budget law for 2021 (the Budget Law)¹ introduced a series of tax measures to generate economic stimulus in the local market.

The most relevant tax measures contained in the Budget Law relate to:

- i. Tax step-up of goodwill and other intangibles
- ii. Tax step-up of Italian participations by foreign shareholders
- iii. Withholding tax exemption on dividends and capital gains for European Union (EU)/European Economic Area (EEA) investment funds
- iv. Tax credit for the purchase of new assets
- v. Reduced taxation of dividends for non-commercial entities
- vi. Extension of tax credits for building renovation
- vii. Tax benefits for selected business aggregations
- viii. Tax credit for investment plans for Italian resident individuals
- ix. Extension of Advance Pricing Agreements (APAs) rollback

Detailed discussion

Tax step-up of goodwill and other intangibles

Law Decree n. 104/2020 (August Decree)² had revamped an opportunity to step-up the value of certain business assets (i.e., land, certain real estate properties, equipment, patents, trademarks and other intangibles) and participations in the financial statements of Italian companies for the period following the one ongoing as of 31 December 2019, i.e., for the fiscal year (FY) ending 31 December 2020 for calendar year entities.

The step-up is available for:

- ▶ Accounting purposes only (**Accounting Step-Up**)
- ▶ Both accounting and tax purposes (**Accounting and Tax Step-Up**)
- ▶ Tax purposes only to align the tax basis of the qualifying assets to their higher accounting value (**Tax Realignment**)

Such election can still be exercised during 2021 until FY20 financials are approved (for the Accounting Step-Up and the Tax Step-Up) or even until the deadline for the FY20 income tax balance payment (for the Tax Realignment).

While any Accounting Step-Up can be made for free, a 3% substitute tax computed on the stepped-up amount is required in the case of an Accounting and Tax Step-Up as well as in the case of Tax Realignment.³ The 3% substitute tax payment can be made in three equal annual installments by the deadline for the annual balance payment of income taxes (which is currently set for the end of the sixth month following the closing of the FY). In such case, the stepped-up value is recognized for IRES (*Imposta sul Reddito delle Società*, i.e., Corporate Income Tax or CIT) and IRAP (*Imposta Regionale sulle Attività Produttive*, i.e., Local Tax) as of the FY following the FY of the election (i.e., the step-up elected with reference to FY20 is effective from 1 January 2021).

In the case of a disposal of stepped-up assets, there is a “claw back” period of three years, meaning that assets disposed of before 1 January 2024 will retain their original tax basis when calculating the related capital gain/loss.

Moreover, in the case of a tax step-up (i.e., in the case of an Accounting and Tax Step-Up as well as in the case of Tax Realignment), a corresponding amount (net of the 3% tax), needs to be registered in the net equity as a revaluation reserve. If such reserve is distributed to the shareholders, an increasing adjustment to the taxable income for the same

amount is triggered. It is however possible to elect for the tax recognition of the said reserve by paying a substitute tax equal to 10% of the amount of the reserve.

The Budget Law extends the scope of the Tax Realignment to goodwill and other intangible assets without legal protection (i.e., expenses relating to several years) resulting from the financial statements ongoing as of 31 December 2019.

Thus, Italian companies recognizing goodwill for accounting purposes, but not for tax purposes (e.g., as a consequence of some past tax neutral reorganizations or revaluations with no tax recognition), have the opportunity to recognize goodwill also for tax purposes and benefit from the related tax amortization going forward.

While the Accounting Step-Up and the Accounting and Tax Step-Up are only available to Italian companies adopting Italian Generally Accepted Accounting Principles (ITA GAAP), the Tax Realignment is also available to companies under International Financial Reporting Standards (IFRS).

Tax-step up of Italian participations by foreign shareholders

The Budget Law revamps an opportunity for resident individuals and nonresident entities (not owning the relevant participation via an Italian permanent establishment) to elect for a tax step-up of participations in unlisted Italian companies and land held as of 1 January 2021 through the payment of an 11% substitute tax.

The provision may be of specific interest to foreign entities which could realize a capital gain subject to corporate income tax in Italy (at 26%) and not be eligible for exemption under an applicable bilateral tax treaty.

The basis of the substitute tax is represented by the value of the participation as of 1 January 2021 and needs to be certified by a sworn appraisal prepared no later than 30 June 2021.

The substitute tax may be either paid in full by 30 June 2021 or through three annual installments beginning 30 June 2021.

Withholding tax exemption on dividends and capital gains for EU/EEA investment funds

The Budget Law introduces an exemption from the Italian withholding tax on dividends and capital gains for selected EU/EEA investment funds.

Investment funds established in EU or EEA countries allowing exchange of information, either compliant with the UCITS⁴ IV Directive or if not UCITS compliant, with a manager subject to regulatory supervision in the foreign country of establishment under the AIFM Directive,⁵ are exempt from:

- i. The 26% withholding tax on Italian source dividends
- ii. The 26% substitute tax on capital gains arising from the disposal of Italian shares, either listed or not, representing a substantial participation

The new measure expands the dividend and capital gain exemptions currently provided for Italian funds to EU/EEA funds, thus avoiding the risk of possible infringement procedures by the European Commission pursuant to the EU non-discrimination principles.

The new exemptions for EU/EEA funds are applicable to dividends paid and capital gains realized from 1 January 2021 onward.

Tax credit for the purchase of new assets

The Budget Law extends the previously available tax credit for government Industry 4.0 Plan high-tech investments for the purchase of new tangible assets (including the ones previously covered by extra-amortization) and certain intangible assets.

In order to qualify for this measure, the Budget Law sets forth that the assets have to be purchased during the period of 16 November 2020 to 31 December 2021, or even until 30 June 2022, provided that purchase orders are accepted by the seller by 31 December 2021 and at least 20% of their price is paid by the same date.

The measure of the benefit applies as follows:

- (i) **For new tangible assets** the tax credit amounts to 10% (15% for investments related to smart working) of the purchase cost with a maximum annual investment amount of €2 million
- (ii) **For new intangible assets** the tax credit amounts to 10% (15% for investments related to smart working) of the purchase cost with a maximum annual investment amount of €1 million
- (iii) **For new high-tech assets**, qualifying under the Industry 4.0 Plan (included in Annex A of Law n. 232/2016), the tax credit amounts to: (i) 50% of the purchase cost for investments up to €2.5 million; (ii) 30% of the

purchase cost for investments from €2.5 to €10 million; and (iii) 10% of the purchase cost for investments from €10 to €20 million. No additional tax credit is provided for investments over €20 million

- (iv) **For new software related investments** (i.e., software, information technology systems and platforms) related to the Industry 4.0 Plan (included in Annex B of Law. No. 232/2016), the tax credit amounts to 20% of the purchase cost with a maximum annual investment amount of €1 million (considering also the investments made in the timeframe 2022-2023 better described in the following paragraph)

The Budget Law also provides for an extension of the tax benefit for assets that will be purchased during the period of 1 January 2022 through 31 December 2022, or even until 30 June 2023, provided that purchase orders are accepted by the seller by 31 December 2022 and at least 20% of their price is paid by the same date. In that case, the measure of the benefit applies as follows:

- (i) **For new tangible assets** the tax credit amounts to 6% of the purchase cost with a maximum annual investment amount of €2 million
- (ii) **For new intangible assets** the tax credit amounts to 6% of the purchase cost with a maximum annual investment amount of €1 million
- (iii) **For new high-tech assets**, qualifying under the Industry 4.0 Plan (included in Annex A of Law. No. 232/2016), the tax credit amounts to: (i) 40% of the purchase cost for investments up to €2.5 million; (ii) 20% of the purchase cost for investments from €2.5 to €10 million; and (iii) 10% of the purchase cost for investments from €10 to €20 million. No additional tax credit is provided for investments over €20 million
- (iv) **For new software related investments** (i.e., software, information technology systems and platforms) related to the Industry 4.0 Plan (included in Annex B of Law. No. 232/2016), the tax credit amounts to 20% of the purchase cost with a maximum annual investment amount of €1 million (considering also the investments made in the timeframe 2021-2022 previously described)

The tax credit applies in three equal annual installments as of the year in which the assets come into operation (and have met the requirements provided by the Industry 4.0 Plan).

Furthermore, a third-party sworn appraisal is required in the case of any Industry 4.0 Plan purchase (high-tech and software related) with a value higher than €300,000.

Reduced taxation of dividends for non-commercial entities

As of FY 2021, dividends will be excluded in the amount of 50% from the Italian CIT base of non-commercial entities (including Italian permanent establishments of foreign non-commercial entities).

To qualify for this favorable tax regime, the non-commercial entities shall jointly meet the following requirements:

- i. They shall exclusively or principally carry out one or more qualifying non-profit activities of general interest for civic, solidarity and social purposes - e.g., family and related values, crime prevention and public safety, scientific and technological research.
- ii. They shall use the related tax savings to finance the mentioned general interest activities, allocating it in a non-distributable and indivisible reserve.

However, this favorable tax regime is not applicable to dividends generated from low-tax jurisdictions.

Extension of tax credits for building renovation

The Budget Law extends to 31 December 2021 the beneficial regime consisting in a tax deduction connected with expenses incurred for qualifying works including: (i) energy requalification works; (ii) building renovation works; (iii) purchase of furniture; (iv) purchase of large low-energy consumption appliances aimed at furnishing the renovated building; and (v) the recovery or restoration of the external facade of existing buildings.

The Budget Law also extends to 30 June 2022 the beneficial regime consisting in a tax deduction for specific qualifying energy efficiency and anti-seismic works (so-called "Superbonus").

Such amendments represent a development of the provisions enacted by Italy with the "Relaunch Decree."⁶ Based on such provisions, the tax deductions connected with expenses incurred for qualifying works (including some of those mentioned above) may be converted either in:

- (a) A transferable tax credit
- (b) A discount of the relevant cost applied by the service provider (in such case, the transferable tax credit is granted to the service provider)

Tax benefits for selected business aggregations

The Budget Law introduces tax benefits for selected business aggregations between third parties including merger and de-merger transactions as well as business contributions implemented through 2021.

The receiving entities involved in the aggregation may elect for the conversion into a tax credit of the deferred tax assets (DTAs) related to the tax losses carried forward and excess Italian notional interest deduction (NID).

The threshold of the convertible DTAs is generally 2% of the sum of the assets of the entities involved (but excluding the entity with most valuable assets).

For such purposes it is not required that the convertible DTAs be recorded in the financial statements.

The companies involved in the relevant business aggregation should, among others:

- i. Be active for at least two years.
- ii. Not be part of the same group, nor be linked by a shareholding relationship greater than 20% or (indirectly) controlled by the same person as per Article 2359(1)(1) of the Italian Civil Code, at the date of the relevant business aggregation and in the two previous years. However, this condition is not required where the control of the involved entities is achieved during 2021 and the aggregation occurs within one year from the acquisition of the control.

The Tax Credit generated upon conversion of the DTAs can be: (i) offset against every kind of tax liabilities and social contributions; (ii) sold; or (iii) requested for refund from the Italian tax authorities.

The conversion of the DTAs becomes effective upon the payment of a tax-deductible fee, equal to 25% of the total amount of the converted DTAs.

Tax credit for Alternative PIRs

For investment plans for Italian resident individuals (*Piani Individuali di Risparmio* - PIR) established under Article 13-bis of Law Decree 124/2019 (Alternative PIRs), the Budget Law introduces a tax credit for losses, capital losses and negative differentials arising from qualifying financial instruments, provided that they are held for at least five years and the tax credit does not exceed 20% of the amounts invested in these financial instruments.

Such tax credit does not represent a taxable income and can be used, in 10 equal annual installments, in the relevant income tax returns or by means of compensation (through the F24 payment form).

This new provision applies to Alternative PIRs set up as of 1 January 2021 for investments made by 31 December 2021.

Extension of rollback of APAs

In line with the international best practice, the Budget Law introduces an extension of the rollback of APAs available to international enterprises for managing in advance selected tax risks.

The rollback of all the unilateral, bilateral and multilateral APAs will be conformed, extending the respective APA to the fiscal year still open to assessment by the Italian tax authorities under the relevant statute of limitations.

The rollback mechanism applies through the amendment of past tax returns and the payment settlement of any additional income tax due in light of the APA. No administrative penalty can be imposed in this respect.

The rollback does not apply where: (i) issues covered by the APA are addressed by investigations or tax assessments served for such FYs; (ii) the foreign competent authorities does not agree to extend bilateral or multilateral APAs; or (iii) the circumstances during the past FYs are different from those considered in the APA.

Moreover, for filing an APA ruling request before the Italian tax authorities the enterprise shall pay a fee equal to:

- (i) €10,000 where the overall turnover of the group is lower than €100 million
- (ii) €30,000 where the overall turnover of the group is higher than €100 million and lower than €750 million
- (iii) €50,000 where the overall turnover of the group is higher than €750 million.

Endnotes

1. Law n. 178 of 30 December 2020 published in the *Official Gazette* on 30 December 2020.
2. Published in the *Official Gazette* on 14 August 2020.
3. Previous versions of the same provision provided for much higher substitute tax rates (i.e., 10% for non-amortizable assets and 12% for amortizable assets) and required to step up entire categories of assets while the current provision allows to pick and chose even a single item.
4. UCITS: Undertakings for the Collective Investment in Transferable Securities.
5. AIFM: **Alternative Investment Fund Manager**.
6. See EY Global Tax Alert, [Italy enacts "Relaunch Decree" to further manage COVID-19](#), dated 27 May 2020.

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