

Italy approves 2019 budget law

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Executive summary

On 29 December 2018, the Italian Parliament approved the 2019 Budget Law, Law n. 145 of 2018 published on the *Official Gazette* of 31 December 2018, (the Law).

The Law includes the following tax measures that may be of interest to multinationals with Italian operations:

1. Introduction of a reduced Corporate Income Tax (CIT) at 15% on the income reinvested in certain new fixed assets and for the creation of jobs
2. Repeal of the Notional Interest Deduction (NID) benefit
3. Introduction of a new tax on digital services
4. Amendments to the extra-amortization regime
5. Review of the tax credit for Research and Development (R&D)
6. Revamping of a special regime to step up Italian participations
7. Revamping of a special regime to step up business assets
8. Clarifications on the Registration Tax
9. Restatement of full deductibility of interest on mortgages of real estate companies
10. Deductibility of Municipal Property Tax (IMU)

Detailed discussion

Reduced corporate income tax at 15%

As of the Fiscal Year (FY) following the one in course on 31 December 2018 (i.e., FY2019 for calendar year entities), companies meeting certain prerequisites will benefit from a reduction of the standard 24% CIT (IRES) by nine percentage points on a portion of their income. Specifically, a reduced 15% CIT rate will apply to a portion of income computed on the lower of: (i) the previous FY's profits set aside for balance sheet reserves (other than non-distributable reserves); or (ii) the total of investments into new fixed assets and costs to hire new personnel.

In this respect, "investments" mean the construction of new plants in Italy (including the completion of suspended works, the expansion, reactivation and modernization of existing plants) as well as the purchase of new tangible assets to be allocated to structures located in Italy (however, investments in real estate, intangibles and vehicles attributed to employees as a fringe benefit are excluded). The portion of the "investment" qualifying for the reduced CIT rate for each FY is based on the tax depreciation of the new assets acquired as of 1 January 2019, within the limit of the increase of the tax basis in the overall fixed assets as compared to 31 December 2018.

With respect to costs related to "new personnel," an increase is required in the average number of total employees working in Italy compared to the number of employees hired as at 30 September 2018, within the limit of the overall increase in personnel costs recorded in the company's income statement for FY2018. The qualifying increase should be computed net of any employment decrease.

The Law provides detailed rules to carry forward under different circumstances any excess of retained earnings as well as of qualifying investments and costs for personnel.

Repeal of the NID

The 2019 Budget Law repeals the NID, currently set at 1.5% of qualifying capital increase. However, taxpayers are still allowed to carry forward and use the excess NID as of 31 December 2018.

New Tax on Digital Services

The Law introduces a new tax applicable to the provision of digital services (the so-called Italian Digital Services Tax or Italian DST) by repealing the old measure introduced by the 2018 Budget Law but never entered into force.¹

According to the new rules, the Italian DST shall now be due by both individuals and enterprises (both resident or nonresident in Italy) carrying on business activities that, individually or at the group level, jointly meet during the fiscal year the following thresholds (the Taxable Persons):

- ▶ Total amount of revenues (wherever arising) not lower than €750,000,000
- ▶ An amount of revenue derived from digital services (arising in Italy only) not lower than €5,500,000

The Italian DST shall be applied only to revenues derived from the following digital services (the Digital Services):

- a) Provision of advertising on a digital interface targeted to users of the same interface
- b) Provision of a digital multilateral interface aimed at allowing users to interact (also in order to facilitate the direct exchange of good and services)
- c) Transmission of data collected from users and generated by the use of a digital interface

An implementing Decree should be issued within four months following the entry into force of the Italian Budget law for 2019 (i.e., by 30 April 2019).

The Italian DST is not applicable yet but it should enter into force starting from the 60th day following that of the publication of the implementing Decree (i.e., accordingly, it should be applicable starting from 30 June 2019).

A separate EY Global Tax Alert will be issued on this development.

Amendments to the extra-amortization regime

With regard to the extra-amortization related to the purchase cost of new high-tech tangible assets which are 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,² the Law sets forth that the investments have to be made by 31 December 2019, or by 31 December 2020, provided that purchase orders are accepted by the seller by 31 December 2019 and at least 20% of their price is paid by the same date.

For FY 2019, the additional amortization amounts to:

- ▶ 170% for investments up to €2.5 million
- ▶ 100% for investments from €2.5 to €10 million
- ▶ 50% for investments from €10 to €20 million

No additional amortization is provided for investments over €20 million.

The additional 40% extra-amortization for certain intangible assets introduced by the Budget Law of 2017,³ is also extended under the same conditions described above.

Tax credit for R&D

The 2019 Budget Law amends the R&D credit by reducing the general applicable rate from 50% to 25%. Specifically, starting from 2019, while the tax credit will be applied generally in the amount of 25%, a 50% rate is applied only to: (i) expenses incurred with respect to R&D contracts signed with universities, and research organizations as well as with independent innovative start-ups and Small and Medium Enterprises (SMEs); and (ii) expenses for employees directly hired to carry out R&D activities.

The maximum annual amount of the tax credit granted to each company will be €10 million (instead of the previous €20 million).

The 2019 Budget Law introduces the obligation, starting from FY 2018, to:

- ▶ Certify qualifying expenses for the purposes of calculating the benefit (that is currently compulsory only for companies that are not legally required to carry out statutory audits).
- ▶ Prepare a technical report illustrating the R&D projects; their progress and all the relevant information for identifying the works eligible for tax credit has been introduced.

Revamping of a special regime to step-up Italian participations

The 2019 Budget Law revamps a one-off opportunity for resident individuals and nonresident entities to elect for a tax step-up of participations in unlisted Italian companies held as of 1 January 2019 through the payment of a substitute tax.

The provision may be of specific interest to foreign entities which could realize a capital gain subject to tax in Italy and not be eligible for exemption under an applicable treaty.

The basis of the substitute tax is represented by the value of the participation as of 1 January 2019 and needs to be certified by a sworn appraisal prepared no later than 30 June 2019.

The substitute tax amounts to 10% for minority interests and to 11% for majority interests i.e., shareholding exceeding 20% of the voting rights (2% for listed companies) or 25% of the share capital (5% for listed companies).

The substitute tax may be either paid in full by 30 June 2019 or through three annual installments beginning 30 June 2019.

Revamping of a special regime to step up business assets

The Law revamps a one-off opportunity for Italian accounting principles adopter companies (ITA GAAP companies) to step up business assets for accounting and tax purposes.

The election may apply to tangible and intangible assets (except for trade goods and immovable properties held by real estate trading companies) as well as to qualifying shareholdings (i.e., controlling shareholding accounted for as financial assets), provided that the mentioned assets are included in the balance sheet related to the period on going on 31 December 2017.

The step up is to be made in the FY18 Financial Statement.

Under the proposed regime, companies can pick and choose the category to be stepped up (however, all the assets belonging to same category shall be stepped up once the category has been chosen) through the payment of a substitute tax amounting to 16% for amortizable/depreciable assets and 12% for non-amortizable/non-depreciable assets. The payment of the substitute tax results in a higher tax base allowing depreciation/amortization at a 27.9% rate or a lower taxable gain in the case of disposal of the assets.

Tax recognition of the new values for depreciation and amortization purposes occurs starting from the third fiscal year following the one in which the step up was made (e.g., from 1 January 2021 for calendar year companies). Tax recognition for capital gain purposes occurs starting from the fourth year following the one in which the step up was made (e.g., from 1 January 2022 for calendar year companies).

The equity reserve created as a consequence of the accounting step up can be freely distributed provided that a 10% substitute tax is paid.

The step up is granted only to ITA GAAP companies. Italian companies reporting under International Financial Reporting Standards (IFRS) are not eligible to make the election for the above step up.

The Law also allows the step up in order to align the tax value of the assets to their accounting value. The substitute tax and the recognition timing are the same as those provided

for the revaluation with the only exception of immovable properties for which the higher values are recognized starting from the FY ongoing on 1 December 2020.

The re-alignment is also available for IAS/IFRS companies.

Clarifications on Registration Tax

The Law expressly qualifies the change introduced by the 2018 Budget Law to Article 20 of the Registration Tax Code as an “authentic interpretation” of the existing provision. This means that the change introduced last year (originally applicable only to events occurred as of 1 January 2018) now has a retroactive effect, i.e., also to transactions that took place prior to 2018.⁴

The 2018 change had reversed the traditional position of the Italian Courts and Tax Administration by stating that the correct Registration Tax treatment of a transaction has to be based on the nature of each single deed to be registered, and regardless of any external interpretative elements (e.g., the behaviors assumed by the parties) or the contents included in other legal transactions which might be “linked” to the one to be registered. Subsequent clarifications had confirmed that the new rule only applied to facts occurred after its entry into force, e.g., with the result that taxpayers hit by assessments recasting the sale of a participation (subject to €200 Registration Tax) into a straight sale of a business (generally subject to 3% Registration Tax) could not rely on such new rule.

The amendment introduced by the Law now allows pre-2018 transactions to benefit from the mentioned change.

Full deductibility of interest on mortgages of real estate companies

The 2019 Budget Law restores the full deductibility of interest on mortgages of real estate companies, previously repealed by Legislative Decree n. 142/2018 (Legislative Decree implementing the European Union Anti-Tax Avoidance Directive).⁵

Real estate companies are defined as companies meeting the following criteria:

- a) The value of the assets reported in the balance sheet mainly refers to the normal value of the buildings to be leased.
- b) At least two-thirds of the revenues arise from the rentals of the buildings.

IMU deductibility

The 2019 Budget Law provides for the increase from 20% to 40% of the deductibility from business income and self-employment income of the municipal property tax (IMU) relating to immovable properties qualifying as capital assets (i.e., not trade assets).

Endnotes

1. See EY Global Tax Alert, [Italy enacts Web Tax and PE definition](#), dated 29 December 2017.
2. See EY Global Tax Alert, [Italian Parliament approves 2017 budget law](#), dated 16 December 2016.
3. Ibid.
4. See EY Global Tax Alert, [Italy approves 2018 Budget Law](#), dated 29 December 2017.
5. See EY Global Tax Alert, [Italy officially releases ATAD decree](#), dated 2 January 2019.

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