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Brief

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The impact to date of the OECD's BEPS project on Italy legislation and audits/ tax enquiries.

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1. The legislative changes made/proposed relating to the BEPS Action Plan.

1.1. Patent Box regime.

The 2015 Budget introduced a patent box regime, which grants a percentage exemption on income derived from the exploitation or the direct use of a qualifying IP both for CIT and IRAP.

The regime is in line with the OECD ‘nexus approach” as described in the reports released on BEPS. The only feature of the Italian rules which is not in line with the OECD principles is the inclusion of trademarks within the scope of intangibles qualifying for the incentive.

1.2. Hybrid mismatch anti-abuse legislation.

Italy has introduced a rule to limit the effect of hybrid mismatches, where income paid by a foreign company to an Italian shareholder (on shares or any form of securities or similar hybrid instruments) may only be taxable as a “divided” (and therefore substantially tax exempt) if it can be demonstrated income of the foreign company.

1.3. Controlled foreign company (CFC) regulation.

In September 2015 Italy has revised the anti-avoidance provisions on CTCs:

- Limitation of the applicability of CFC rules to controlled companies (and no longer for affiliated companies);
- repeal of the mandatory ruling procedure required to obtain exemption from the application of CFC rules (the ruling remains an option). “Business” test or “subject to substantial tax” test can be documented in case of tax audit.

1.4. Additional legislation.

In August 2015, Italy approved rules that technically define the concept of “abuse of law”, according to the rules on aggressive tax planning provided by Recommendation n. 772/2012/UE. Taxpayers may ask for a general ruling to determine

if the transactions that they are about to carry out may constitute abuse of law. No criminal charges would be linked to the "abuse of law" behavior. Recent changes in the law seems to exclude the concept of criminal offences for the legal representatives in case of TP evaluation issues. New types of ruling were introduced in order to facilitate a common tax approach between Taxpayers and Tax Authorities, including those for companies with considerable investments in Italy (EUR 30M) and effects on the levels of employees involved. An optional branch exemption regime has also been included.

2. About how the initiative impacted tax enquiries/audit.

In Italy's experience, the audit force is continuing to target large multinational organizations within Italy.

A specific division within the tax authority has been created in each region devoted to controls and auditing of "large taxpayers", which are defined as companies with a turnover exceeding EUR 100m. The tax inspectors within this specialized division are generally high level staff who have received significant training on various tax avoidance/evasion schemes. A such these specific regional divisions are becoming increasingly efficient and effective in targeting such schemes as part of their audits.

Specific areas of challenge are regarding the existence of hidden Permanent Establishments (PEs) (RELATING TO Action 7 of BEPS) and treaty abuses (Action 6). Additionally transfer pricing issues are subject to even increasing challenges, not only through the use of TP adjustments but also on the basis of re-characterisation of intercompany loans into capital. The allocation of free capital to the branches of foreign entities Italian tax law has expressly stated that it must be determined according to the OECD principles, bearing in mind performed functions and undertaking risks.

3. The proposing to introduce country-by-country reporting.

Italian 2016 Budget Law introduced CbC reporting. The regulations are to a great extent in line with the BEPS Action 13 deliverables. An implementing decree will be issued in order to specify procedural aspects.

4. The reaction to the propose BEPS initiatives regarding interest deducibility.

The Italian tax legislation regarding interest deducibility has been modified in 2007 where a 30% EBITDA passive interest limitation has been introduced. Beginning in 2016, dividends cashed in form non-Italian resident controlled companies will be included in the EBITDA computation, and will no longer be included in the consolidation tax systems the EBITDA of the non –Italian controlled companies.

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Palma Boria law firm is fully available to support all the clients who are interested in the evaluation of the legal and tax impact in Italy related to the BEPS Action Plan

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