Highlights

- Changes to rules on taxation of crossborder relationships
- New definition of "abuse of law"
- Review of statute of limitations
- Cooperative compliance program

On 21 April 2015 the Government approved a package of measures that will significantly change the Italian tax system.
The draft legislative decrees issued based on framework legislation adopted in 2014 shall become effective shortly.

1. Changes to rules on taxation of crossborder relationships

A first decree ("**International Tax Decree**") amends the rules governing international taxation to make it more competitive. These are the highlights:

- Reshaping of advance ruling programs:
    - extension of the scope of APAs to cover not only transfer pricing matters and tax treaty application issues, but also the determination of entry tax bases or exit taxes in case of inbound and outbound migration of entities and attribution of profits to permanent establishments;
    - introduction of the possibility to roll the outcome of an APA back to the tax period in which the APA application was made, by adjusting tax returns in light of the APA principles, without penalties;
    - new program of advance rulings for new investments (for a value exceeding € 30 million) that have a positive impact on employment. Italian and foreign investors may obtain advance certainty on the applicable tax regime, on transfer pricing, on the absence of abuse and on other material tax issues of the proposed investment based on the investment business plan.
- Rationalisation of CFC rules:
    - repeal of the mandatory ruling procedure required to obtain exemption from the application of CFC rules to foreign subsidiaries (the ruling remains as an optional procedure). Exemption

    - (“business” test or “subject to substantial tax” test) may so be documented in case of tax audit;
    - indirect foreign tax credit on dividends and capital gains derived from “black-list” subsidiaries that were not subjected to CFC rules because they carry out an actual industrial or commercial activity;
    - limitation of the applicability of CFC rules to controlled companies (i.e. repeal of CFC rules for “affiliated” companies, owned for at least 20%, or 10% for listed companies).
- Replacement of existing “blacklist” cost rules:
    - “blacklist” costs will now be deductible to the extent that transactions have been actually executed and that costs do not exceed the fair market value of the goods and services received.
- Fiscal unit:
    - applicability of the fiscal unit regime also to cases where two (or more) Italian resident companies are controlled by a company resident in a EU State without a single Italian-resident controlling company (similarly, Italian permanent establishments of foreign entities can be part of the fiscal unit).
- Introduction of an optional all-in “foreign branch exemption” regime (i.e. with the option must be exercised for all foreign permanent establishments with no time limitations).
- Re-definition of interest deduction rules for Italian groups controlling foreign entities:
    - repeal of the possibility to use foreign controlled companies’ EBITDA for the purposes of determining the maximum deductible amount (30% of EBITDA);
    - inclusion in the relevant EBITDA of dividends received from foreign controlled companies.
- For companies migrating to Italy, possibility to step up the tax basis of assets (in case of migration from a non-white listed State, such step up is subject to an APA).
- Amendment of rules governing debt restructuring:
    - taxability of benefits received by companies due to the waiver of credits by the shareholder to the extent that exceeds the tax basis of the credit, regardless of the accounting treatment;
    - extension of possibility to deduct bad debt losses also in case of foreign procedures equivalent to Italian debt insolvency procedures.

2. Specific definition of “abuse of law” principle and review of the procedural rules related thereto, with the exclusion of the criminal relevance of abusive transactions

Another decree (“Certainty Decree”) entirely reviews the set of anti-avoidance rules and abuse doctrine and introduces a single legal definition of “abuse of law” that will replace all definitions and doctrines previously developed (quite extensively) by the tax authorities and endorsed by case law. Such new definition will also apply retrospectively to transactions which have not yet been challenged by Revenue Agency through a formal deed of assessment.

Under the new rules, abuse of law exists when a transaction “*lacks any economic substance and, while formally consistent with tax law, is aimed at obtaining undue tax advantages*”. The new definition specifies that:

- transactions are regarded as lacking any economic substance when they consist in facts, contracts, deeds, even interconnected, that are unsuitable to generate significant effects other than tax saving;
- undue tax advantages consist in tax benefits, even incurred in the long run, obtained in contrast with the purpose of the tax rules or with the principles of the tax legal system;
- a transaction is not considered to be abusive when it is justified by sound and non-marginal non-tax reasons, even if managerial or organisational, aimed at improving the structure or functionality of the business of the taxpayer;
- the taxpayer is always free to choose between different optional tax regimes provided by the law or between different transactions leading to different tax burden;
- abuse of law can be challenged only if the tax benefits cannot be assessed through other specific tax provisions.

New procedural rules require the Revenue Agency to properly activate a confrontation with the taxpayer and provide evidence of the abuse. Failure to comply with such requirements which makes the assessment void.

It is further provided that tax courts cannot raise *ex-officio* the existence of abuse of law.

Finally, the new definition provides that any abusive conduct does not amount to a criminal behaviour, thereby eliminating the uncertainty on this latter point which had led in the past few years to conflicting case law.

3. Review of statute of limitations

With the Certainty Decree the Government also introduced changes to the statute of limitations rules for tax assessments as follows:

- exclusion of the possibility for the tax authorities to double the statute of limitations, unless a notice of commission of a tax crime has been transmitted to the public prosecutor before the expiry of the ordinary statute of limitations;
- introduction of a grandfathering clause for all assessment notices already served based on the doubling of statute of limitations under the previous (looser) rules.

As a consequence of such change, the power of tax authorities' power to assess past violations for incorrect tax returns will be reduced from 8 years to 4 years from the year of filing of the tax return (except for cases where a criminal violation has been communicated to the public prosecutor before elapse of the fourth year).

4. Cooperative compliance program available to large taxpayers

A new cooperative compliance program is introduced for taxpayers that have processes and internal controls procedures ensuring that tax risks are known, monitored and controlled. Participation to the cooperative compliance program will allow taxpayers to achieve with the Revenue Agency a common evaluation of potential tax risks before filing tax returns.

Even if implementing decrees are still to be issued, the decree states that, in a preliminary phase, the program is reserved to taxpayers with at least € 10 billion turnover and to certain other limited cases.

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