

# PROPOSED LEGISLATION FOR ITALIAN PATENT BOX REGIME

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## Tags

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## INTRODUCTION

Currently, the E.U. and the O.E.C.D. are finalizing new rules for the design of acceptable tax regimes for intangible property (“I.P.”) box companies. The stated intent of this legislation is to promote the development of high-value jobs associated with the creation of I.P. The concern of the E.U. is that the tax benefit is a form of illegal state aid. The concern of the O.E.C.D. is that the real intent behind the patent box tax regimes is to attract movable income to a low tax environment that has no tangible connection to the I.P. or its development. Thus, Action 5 of the B.E.P.S. Action Plan proposes that preferential tax regimes are acceptable only if there is a direct proportionate nexus between the I.P. income and the R&D activity that generated that income.

It is thought the E.U. attack on I.P. box companies is championed by Germany, France, Spain, and Italy. However, Italy recently introduced its own I.P. tax incentive plan, known as a “patent box regime.”

## TAX BENEFITS OF ITALIAN PATENT BOX REGIME

The Italian legislation provides reduced tax – or no tax in some instances – on income derived from qualifying I.P. Businesses are exempt from tax on a percentage of income derived from I.P. The exempt percentage is 30% of income in 2015, 40% in 2016, and 50% in 2017 and later years. Consequently, the standard tax rate of 31.4% will be reduced to 15.7% by 2017. In addition, if I.P. is sold and 90% of the sales proceeds are reinvested in the development of similar I.P. by the end of second fiscal year following the year of sale, the entire gain will be tax-free.

Activities that must be performed in order to benefit from the regime can be performed directly or outsourced under research agreements with various institutions, such as universities or research centers.

Businesses must make an election to apply the regime. The election is irrevocable for five years. Nonetheless, the patent box incentive can be used in conjunction with other Italian tax incentive regimes.

A foreign corporation that has a permanent establishment in Italy can elect the benefits of the patent box regime but only if it is a tax resident of a country that has a tax treaty with Italy containing an exchange of tax information clause.

## ASSETS THAT QUALIFY FOR TREATMENT

Activity related to the development of patents and non-patented I.P. equivalents will give rise to income that qualifies for the incentive program. Purely commercial brands and trademarks are specifically excluded. A carve-out is provided for commercial brands and trademarks that require ongoing R&D expenditure.

Taxpayers must generally enter into an Advanced Pricing Agreement (“A.P.A.”) with the Italian Revenue Agency to access the regime with respect to such aspects as intra-group royalties or intra-group transfers of ownership. The A.P.A. is intended to prevent Italian companies from moving excessive income from a 31.4% tax environment to a 15.7% tax environment. Income from third-party royalties or transfers of ownership does not require an A.P.A.

## UNANSWERED QUESTIONS

The statutory commentary accompanying the Italian legislation makes explicit reference to the nexus requirement mentioned in the B.E.P.S. Action Plan. To receive favorable tax treatment, substantial R&D activity must take place and the income benefitting from reduced tax must be related to that activity. No definitional standard is provided under which activity will be viewed to be substantial. In addition, the types of trademarks that generate income benefitting from the patent box regime has not been explained.

