

“COVID-19” EPIDEMIOLOGIC EMERGENCY

TAX MATTERS – CONVERSION OF DEFERRED TAX ASSETS

The epidemiologic emergency due to the outbreak of “COVID-19”¹ in our country affects, *inter alia*, tax matters.

Following the entry into force of Law Decree No. 11 of March 8, 2020, on March 17, 2020 the Law Decree No. 18 was published in the Official Gazette No. 70 (so called Law Decree “Cura Italia”, hereinafter “Decree”) and entered into force. The Decree sets forth “*Measures aimed at strengthening the National Health Service and providing economic support measures for families, workers, and companies, related to the Covid-19 epidemiologic emergency*”.

Among the measures adopted by the Decree with regard to tax matters, it is worth mentioning art. 55 – “*financial support measure for enterprises*”, which provides for the conversion, at certain conditions, of deferred tax assets (“DTAs”) into a tax credit (“Tax Credit”).

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¹ Covid-19 is the acronym for the respiratory disease due to the new coronavirus. Such acronym is the combination of “Corona”, “Virus”, “Disease”, as well as 2019 as year of identification. The virus has been labelled “Severe Acute Respiratory Syndrome 2” or “SARS-CoV-2”. Further information are available on the institutional website of the Ministry of Health: <http://www.salute.gov.it/>



Associazione professionale tra

Avv. Stefano Bianchi - Avv. Daniele Carminati - Avv. Claudio Cera - Avv. Enrico Del Guerra - Avv. Mario Di Giulio - Avv. Gian Paolo Di Santo
Avv. Filippo Fioretti – Avv. Marco Giustiniani - Avv. Vittorio Loi - Avv. Francesco Manara - Avv. Nico Moravia - Avv. Mia Rinetti - Avv. Meritxell Roca Ortega
Avv. Marina Santarelli - Avv. Maurizio Vasciminni - Avv. Sven von Mensenkampff - Avv. Roberto Zanchi e Dott. Marco Jannon

Soci Onorari: Agostino Migone de Amicis - Bruno R. Pavia

C.F. - P.I. (V.A.T. N.) 01771720156

1. Measures to support the liquidity of companies and workers

1.1. *Legal Framework*

Article 55 of the Decree, while providing for the complete amendment of article 44-*bis* of Decree Law no. 34 of April 30, 2019, introduced a new special conversion regime for DTAs.

In particular, companies that transfer for valuable consideration by December 31, 2020 receivables, either commercial or deriving from financing, claimed from defaulting debtors², may convert into a Tax Credit the DTAs relating to:

- tax losses carried forward (“NOLs”), not yet counted as a reduction in taxable income at the date of the transfer;
- notional interest deduction (“NID”) surpluses, not yet used or deducted from taxable income at the date of the transfer;

not exceeding 20% of the nominal value of the transferred receivables (the latter may not exceed Euro 2 billion³).

The conversion into a Tax Credit may take place even if the DTAs have not been recorded in the financial statement (for example, for failure to pass the so called “*probability test*”⁴) as long as they relate to NOLs and NID surpluses not yet deducted or used at the date of the transfer of the receivables.

It has to be noted that both NOLs and NID can off-set the taxable income only for corporate income tax (“IRES”) purposes. Then the mentioned tax assets can generate only DTAs calculated applying the IRES tax rate (i.e. 24% for companies and 27,5% for banks and other financial institutions).

Are excluded from the aforementioned incentive:

- companies for which the state or risk of bankruptcy or insolvency has been established, as defined by the relevant regulations;
- transfer of receivables between companies linked by control relationships pursuant to article 2359 of the Italian Civil Code and to companies controlled, even indirectly, by the same party.

Moreover, from the effective date of the transfer of the receivables, it will no longer be possible to decrease the taxable income using NOLs and NID surpluses in the amount attributable to DTAs subject to conversion into a Tax Credit⁵.

² For the purposes of the provision, a default occurs when the non-payment lasts for more than 90 days from the date on which it was due.

³ This limit is to be calculated at an aggregate level for companies that are linked by a control relationship within the meaning of article 2359 of the Italian Civil Code and for companies controlled, even indirectly, by the same party.

⁴ According to the provision of the Italian GAAP no. 25 issued by OIC (i.e. the Italian standard setter).

⁵ We underline that it is still not clear if the relevant NOLs and NID should be those existing as of December 31, 2019 or, on the contrary, those existing at the date of the transfer of receivables. This is one of the points for which clarifications from the Italian Tax Authorities (“ITAs”) are awaited.

The loss recorded following to the transfer of the receivables is still deductible for tax purposes.

1.2. Exercise of the option

In order to convert DTAs into a Tax Credit, the transferor must exercise the option provided for in Article 11, paragraph 1, of Law Decree No. 59 of May 3, 2016.

In particular, it should be an irrevocable option, to be exercised by the end of the current fiscal year in which the transfer of the receivables takes effect, till the fiscal year 2030.

The option is subject to the payment of an yearly fee⁶ equal to 1,5% of the difference (if positive) between DTAs eligible for conversion accrued starting from fiscal year 2008 and taxes paid starting from fiscal year 2008. In case of negative difference the DTAs guarantee fee is not due.

The option become effective, alternatively:

- with the payment of the fee; or
- if the fee is not due, following to the filing of a communication via PEC to the *Direzione Regionale dell'Agenzia delle Entrate*.

The conversion of the DTAs is allowed if the mentioned option is exercised by the end of the tax period in which the receivables are transfer, and it is effective starting from the following fiscal year⁷.

The yearly fee has to be paid within the deadline for the payment of corporate income tax balance due for the previous fiscal year. The fee is deductible from IRES and IRAP in the fiscal year in which it is paid.

1.3. Use of the Tax Credit

The Tax Credit must be indicated in the UNICO tax return.

Since the day of efficacy of the sale of receivables, the taxpayer is entitled to:

- offset the Tax Credit versus other taxes without any threshold to the off-set⁸;
- sale the Tax Credit to third parties. In this case the transferred credit may be used by the transferee only after the transferor has indicated it in the tax return;
- claim for a refund of the Tax Credit;
- transfer the Tax Credit to group companies according to art. 43-*bis* and 43-*ter* of the Presidential Decree no. 602/73.

⁶ Introduced by art. 11, paragraph 1 of Law Decree no. 59/2016 of May 3, 2016.

⁷ Another point still uncertain is the timing for the use of the Tax Credit. According to a more restrictive interpretation of art. 55, the Tax Credit should be use from January 1, 2021. According to a second interpretation the Tax Credit could be utilised from the date of the transfer of the receivables. Even in this case we wait for further clarifications from the ITAs.

⁸ Generally, the total amount of so-called "horizontal offset" (i.e. a tax can be used to offset debits arisen with respect to another tax) during a fiscal year cannot exceed the threshold of Euro 700,000.

1.4. Numerical Example

		Example 1	Example 2
A	Carry forward tax losses	1,000,000	1,000,000
B	NID surpluses	400,000	400,000
C = A + B	Total relevant tax assets	1,400,000	1,400,000
D	Nominal value of transferred receivables	(*)10,000,000	(*)10,000,000
E	Whose intercompany	-	5,000,000
F = D - E	Net receivables ex art. 55	10,000,000	5,000,000
G	Price of transfer of receivables	5,000,000	5,000,000
H = F*20%	Maximum amount of relevant tax assets	2,000,000	1,000,000
I = lower between C and H		1,400,000	1,000,000
Convertible DTAs (I*24%) (**)		336,000	240,000
Losses on receivables deductible (D-G)		5,000,000	5,000,000

(*) We assumed the same face/tax value for the receivables.

(**) We assumed the corporate income tax rate for industrial and commercial companies.

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