Italy issues the new Patent Box implementation decree

Tax Alert
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Offices

Milan
Via Vittor Pisani 27, 20124
T: +39 02 676441 - F: +39 02 67644758

Ancona
Via I° Maggio 150/a, 60131
T: +39 071 2916378 - F: +39 071 2916221

Bologna
Via Innocenzo Malvasia 6, 40131
T: +39 051 4392711 - F: +39 051 4392799

Florence
Viale Niccolò Machiavelli 29, 50125
T: +39 055 261961 - F: +39 055 2619666

Genoa
P.zza della Vittoria 15/12, 16121
T: +39 010 5702225 - F: +39 010 584670

Naples
Via F. Caracciolo 17, 80122
T: +39 081 662617 - F: +39 081 2488373

Padua
Piazza Salvemini 2, 35131
T: +39 049 8239611 - F: +39 049 8239666

Perugia
Via Campo di Marte 19, 06124
T: +39 075 5734518 - F: +39 075 5723783

Pescara
P.zza Duca D'Aosta 31, 65121
T: +39 085 4210479 - F: +39 085 4429900

Rome
Via Adelaide Ristori 38, 00197
T: +39 06 809631 - F: +39 06 8077459

Turin
C.so Vittorio Emanuele II 48, 10123
T: +39 011 883166 - F: +39 011 8395865

Verona
Via Leone Pancaldo 68, 37138
T: +39 045 8114111 - F: +39 045 8114390

Introduction

A ministerial decree, issued on 28 November 2017 (the 'Decree'), revises the rules implementing the optional tax regime providing a partial tax exemption on income arising from the exploitation of qualifying intangible assets ('IP'). This relief is known as the Patent Box regime(1).

The Decree, which replaces the previous one of 30 July 2015(2), follows the amendments made to the Patent Box regime by Law Decree no. 50 of 24 April 2017(3), which excluded trademarks from the list of qualifying IP. Therefore, from tax year 2017, the forms of qualifying IP are:

— software protected by copyright

— patents

— legally protectable designs and models

— legally protectable processes, secret formulas and industrial, commercial or scientific knowledge ('know-how').

The Decree defines certain forms of qualifying IP in more detail, clarifies the Patent Box regime for trademarks until the end of 2016, and provides guidance on the exchange of information about trademarks with other countries.

(1) For a general overview of the Patent Box regime, see our Tax Alert of 2 December 2014 and our Tax Alert of 2 February 2015.

(2) See our Tax Alert of 3 November 2015.

(3) See our Tax Alert of 3 May 2017.

Definition of know how

The Decree confirms the partial misalignment of the Italian Patent Box regime with the OECD recommendations, since the benefit is still available for know-how consisting in processes, secret formulas and industrial, commercial or scientific knowledge. This definition seems to be wider than that found in BEPS Action 5 (4)(II)(b), which states that the only IP assets that could qualify for tax benefits under an IP regime are patents and other IP assets that are functionally equivalent to patents(4).

In Circular 11/E of 11 April 2016, the Italian Revenue Agency clarified the meaning of know-how, citing the definition given in article 1(i) of Commission Regulation (EC) No 772/2004 of 27 April 2004(5).

For the purposes of the Patent Box regime only, know-how is considered as 'legally protectable' if:

a) it is secret, in the sense that it is not, in its entirety or in the precise configuration and combination of its elements, generally known or easily accessible to experts and operators in the sector (this is knowledge that, on its own or in combination, cannot be acquired by an operator in the sector within a reasonable period of time and at a reasonable cost, while its acquisition by a competitor requires effort or investment);

b) its secrecy has economic value and the know-how gives those who use it a competitive advantage that enables them to maintain or increase their market share;

c) the persons who own the know-how adopt reasonably adequate measures to maintain secrecy.

Test data or other secret data which involve a considerable processing effort are also considered as legally protectable know-how(6).

(4) IP assets that are functionally equivalent to patents are:
- i. patents defined broadly;
- ii. copyrighted software;
- iii. other IP assets that are:
  - non-obvious, useful and novel;
  - substantially similar to IP assets in the first two categories;
  - certified as such in a transparent certification process by a competent government agency that is independent from the tax administration.

(5) Know-how means a '*package of non-patented practical information, resulting from experience and testing, which is: (i) secret, that is to say, not generally known or easily accessible, (ii) substantial, that is to say, significant and useful for the production of the contract products, and (iii) identified, that is to say, described in a sufficiently comprehensive manner so as to make it possible to verify that it fulfils the criteria of secrecy and substantiality*'.

(6) Circular 11/E of 7 April 2016.

Grandfathering

Article 13 of the Decree (headed 'Grandfathering') provides that taxpayers who opted for the Patent Box regime for trademarks in the tax years in progress on 31 December 2015 or 31 December 2016 may still take the benefit until 30 June 2021 (not renewable).

Therefore, although BEPS Action 5 recommended that no new options for regimes inconsistent with the OECD principles should be admitted after 30 June 2016, in Italy options exercised between 1 July 2016 and the end of any tax year in progress on 31 December remain in place.

Starting from 2017 (for calendar-year taxpayers), each taxpayer that has exercised the option in relation to trademarks must declare the following in its annual tax return: the number of assets concerned; the classification of those assets; the eligible income for each type of asset.

The annual tax return must also be used to specify the foreign countries in which the following companies are tax resident:

i. the company that exercises direct control over the entity;

ii. the company that exercises indirect control over the entity, if that company is controlled exclusively by the state, other public bodies or individuals, or if that company is not controlled by any entity;

iii. the related companies from which the entity has received remuneration for the exploitation of the trademarks.

Exchange of information

With reference to trademarks, the Decree provides for the exchange of information with those members of the Inclusive Framework on BEPS for which there is an international legal instrument (e.g. EU directive, double taxation convention) that allows exchange.

In such cases, article 14 provides that - within three months of receiving the tax return for the tax periods concerned - the Italian tax authorities must give the name of each entity that has exercised the option for trademarks to the tax administrations of the countries where the entity's controlling and related companies are tax resident.

Document prepared and written by Carlotta Bertù

Contacts

KPMG, Tax & Legal

Fabio Avenale
Partner,
Tax Professional Practice
T: +39 011 883166
E: favenale@kpmg.it

Lorenzo Bellavite
Senior Manager,
International Tax
T: +39 045 8114 111
E: lbellavite@kpmg.it

kpmg.com/it

kpmg.com/socialmedia **kpmg.com/app**

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