

Italian Patent Box Regime

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1. Foreword

The Italian **Patent box regime** provides incentives for the creation and economic exploitation of intangible assets in business activities.

The Patent box regime allows for:

- an increase, for tax purposes, of the costs incurred in carrying out research and development activities aimed at maintaining and developing existing intangible assets (“ordinary regime”). Such extra-deduction is equal to 110% of the costs actually borne;
- the deduction of 110% of the value of the costs incurred in carrying out the research and development activities that contributed to the creation of an intangible asset that has obtained an industrial property title. The eligible expenses are those incurred as of the eighth tax period preceding the one in which the intangible asset obtains an industrial legal protection (“reward mechanism”).

This Patent box regime applies from the fiscal year running on October 22, 2021. From the same fiscal years it is not possible to elect for the previous Patent box regime anymore.

2. Scope of application

The Patent box regime can be applied by persons deriving business income which carry out research and development activities in relation to certain intangible assets (see below).

2.1 Beneficiaries

The Patent box regime can only be applied by persons deriving business income under Italian tax law. Non-resident companies and entities of all types, including trusts, with **permanent establishments** in Italy can benefit from the Patent box regime provided they are resident in countries with which have concluded a **Tax Treaty** with Italy which allows for a satisfactory exchange of information.

The eligible persons can apply the Patent box regime provided that they carry out the research and development activities aimed at the creation and development of intangible assets, including through outsourcing agreements contracts entered into with:

- companies which are not part of their group;
- universities or research institutions and equivalent institutions.

It is also necessary for the eligible person to qualify as an investor and to retain the right to the economic exploitation of the relevant intangible assets.

2.2 Eligible intangible assets

The Patent box regime is aimed at fostering research and development activities incurred in the creation and development of the following intangible assets:

- software protected by copyright;
- patents;
- legally protected models and designs;
- two or more intangible assets among those previously indicated, linked together by a bond of complementarity such that the realization of a product or a kind of products or a process or group of processes is conditional on the joint and complementary use of the same.

For the definition of intangible property and the requirements for its existence and protection, reference is made to national, European Union and international standards and those contained in European Union regulations, treaties and international conventions on industrial and intellectual property applicable in the relevant territory of protection.

Unlike the **previous Patent box regime**, pending patents and design and model registration applications do not fall within the scope of the tax regime.

2.3 Relevant activities

The Patent box regime can be applied provided that enterprises develop the following activities:

- industrial research;
- experimental development;
- technological innovation;
- design and aesthetic creations;
- legal protection of intangible property rights.

For the purpose of applying the reward mechanism, the activities listed below are also of relevance:

- fundamental research;
- design and implementation of copyrighted software.

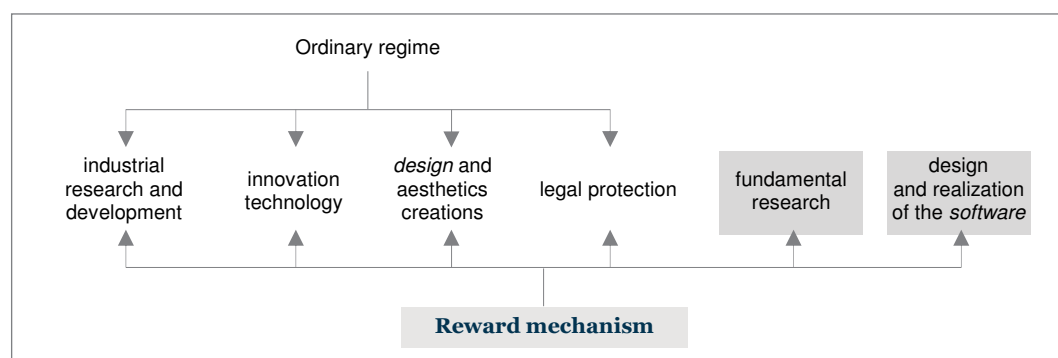


Fig. 1 - Relevant activities for reward mechanism

The definitions of fundamental research, industrial research, innovation technology and design and aesthetic creation activities are contained in decree issued by the Italian Ministry for the Economic Development.

The aforementioned activities must be carried out in laboratories or facilities located in the territory of the Italian state, in EU or EEA Member States having in force an effective exchange of information agreement with Italy or in Countries that allow for a satisfactory exchange of information with Italy. These last Countries are listed in the Ministerial Decree of 4 September 1996.

2.4 Eligible costs

The Patent box regime grants a 110% extra deduction, for tax purposes, with respect to expenses incurred by enterprises carrying out activities aimed at the creation, maintenance and development of eligible intangible assets.

For the purpose of determining the basis of calculation to which the 110% increase is to be applied, the following expenses are relevant:

- salaries and other costs related to employee or self-employed personnel that carried out the relevant activities;
- depreciation costs, financial and operating lease fees and other expenses related to tangible and intangible assets used to carry out such relevant activities;
- consultant's costs;
- costs borne for materials, supplies and other products used in relevant activities.

Legal fees borne in order to prevent the counterfeiting of eligible assets or incurred because of litigation procedures aimed at ascertaining and protecting the rights arising because of the eligible assets are considered to be eligible costs.

For the purposes of the rewarding mechanism, costs incurred in obtaining an industrial property title are considered to be relevant.

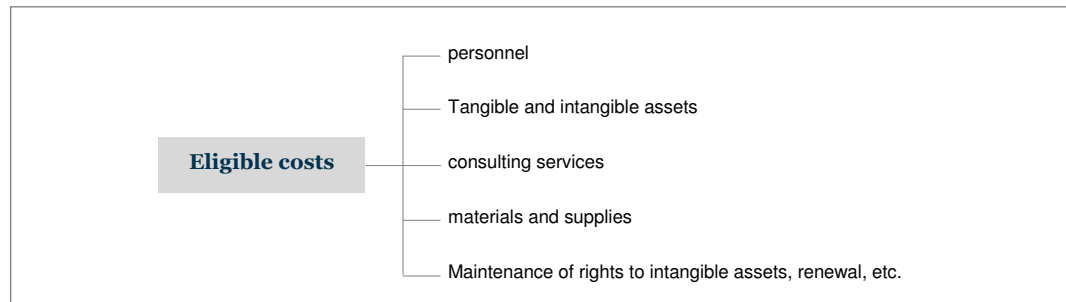


Fig. 2 - Eligible costs

The aforementioned expenses are eligible to the extent that they do not arise from intercompany transactions.

From a temporal standpoint, eligible expenses are relevant for Patent box regime purposes when they are considered to be accrued under the relevant tax rules, regardless to their accounting treatment and to whether they are capitalized or not.

3. Option and eligible amounts

For enterprises applying the Patent box regime, costs incurred in carrying out relevant activities are increased by 110% of their value for:

- **IRES** purposes; and
- **IRAP** purposes.

3.1 Exercise of the option

The election for the Patent box regime must be exercised in the relevant tax return.

Such option:

- lasts for five fiscal years;
- cannot be revoked;
- can be renewed.

3.2 Ordinary regime

The ordinary regime allows for an increase of 110% of the relevant costs borne in calculating the taxable income of the taxpayer.

For example, assuming that an enterprise has incurred research and development costs of 10,000.00 Euros in a given fiscal year, where the Patent box regime applies, the total amount deductible for IRES and IRAP purposes will be 21,000.00 euros.

3.3 Reward mechanism

Where the eligible costs are incurred throughout several fiscal years, enterprises may benefit from the 110% markup of such costs in the fiscal years in which the industrial property title for the relevant asset is obtained.

Costs suffered before the eighth fiscal year prior to the one in which the industrial property title is obtained fall outside the scope of the regime.

Where M&A transactions occur during the observation period referred to above, the person which obtains the industrial property title is the one which can actually benefit from the regime.

4. Documentation

Persons eligible to apply for the Patent box regime may file and store all the relevant documentation needed in order to prove their right to apply it. Where such documentation is maintained, the relevant person needs to flag a specific box of its tax return.

4.1 Purpose of documentation

The preparation and maintainance of the documentation related to the benefit at stake allows the relevant enterprises to benefit from a penalty protection.

In essence, in the event that the Italian Tax Authorities challenge the benefit enjoyed under the regime, the taxpayer may not be subject to any administrative penalty (which will be otherwise applicable with a range of 90 to 180 percent of the higher tax due as a result of the assessment).

4.2 Content of the documentation

To benefit from the penalty protection, the documentation must contain all the data, information and elements specified in Ordinance no. 48243 of 15 February 2022.

The documentation is divided into two sections:

- the first section is aimed at describing the operational and functional context of the enterprise, with particular regard to the kind of activities carried out and the way they were carried out;
- the second section is aimed at validating, supporting and justifying, from an accounting and tax standpoint, the information reported in the previous section. This information should allow the Italian Tax Authorities to verify the correctness of the amount of the benefit.

4.3 Documentation features

The above mentioned documentation must be:

- drafted in Italian, but elements and data that relate to transactions with foreign associated enterprises or foreign third parties may be submitted in English;
- signed by the legal representative of the company or his/her delegate, through an electronic signature with an electronic time stamp. The documentation needs to be signed within the date of submission of the relevant tax return;
- prepared for each fiscal year for which the enterprise has opted for the Patent box regime.

5. Glossary

IRES

Italian Corporate Tax (IRES) with a 24% flat rate, reduced to 12% for some no-profit organizations and increased to 27.5% for banks and other financial institutions.

IRAP

Regional tax on productive activities levied on companies and, until 2021, individual businesses at 3.9% rate (which may vary depending on several factors).

Italian Tax Authorities (Agenzia delle Entrate)

Agency, under control of the Ministry of Finance, which performs all the functions and tasks assigned by the law in the field of tax revenue and tax duties.

Ordinance

Official document issued by the Italian Tax Authorities containing rules aiming at implementing and supplementing provisions of tax law (tax returns, etc.).

Patent Box Regime

It generally indicates a regime aimed at fostering the creation, maintenance, enhancement and

protection of intangible assets. From a tax perspective, these regimes usually allow for a preferential tax regime to be applied to income or costs connected to intangible assets.

Permanent Establishment

In international tax law, it defines the threshold for a presence of foreign enterprise to be taxable in another State. The domestic definition is provided under Art. 162 of the TUIR. This definition is substantially consistent with Art. 5 of the OECD Model Tax Convention.

Previous Patent Box Regime

Optional regime allowing for a reduced taxation of income derived from the use or concession of the use of certain types of intangible assets.

Tax Return

Form that persons need to file and submit yearly to the Italian Tax Authorities in order to declare their Italian income.

Tax Treaty

International Convention concluded between two States for the avoidance of double taxation and double non-taxation in economic transactions involving them.