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WORKING PAPER

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MEETING DOCUMENT

From:	Italian delegation
To:	Working Party on Tax Questions (Direct Taxation – CCTB)
Subject:	Anti-avoidance provisions relating to ACE

Delegations will find attached a document from the Italian delegation on CCTB Article 11 in view of the meeting of the Working Party on Tax Questions (Direct Taxation - CCTB) on the morning of 26 April 2017.

Anti-avoidance provisions relating to ACE

As regards the Italian legislation relating to ACE, Article 10 of the decree of Ministry of Economy and Finance 14 March 2012 (“ACE Decree”) lays down anti-avoidance provisions to prevent, especially within corporate groups, any distortion caused by a multiple granting of the benefit vis-à-vis a single contribution to the equity capital. The intention of the legislator was in fact to prevent that the same amount of cash could increase the equity of several legal entities belonging to the same group of companies.

With respect to intra-group transactions, paragraphs 2 and 3 of the above Article identify the following cases which reduce the ACE *base* (‘sterilization’):

- 1) cash contributions made in favour of residents;
- 2) acquisitions or increments of control participations;
- 3) acquisitions of business or part of a business;
- 4) cash contributions from:
 - entities resident in countries which allow exchange of information for tax purposes if controlled by resident entities;
 - entities resident in countries which do not allow such exchange of information;
- 5) increases of financial credit with respect to the situation resulting from the financial statements for the year ending on 31 December 2010.

The ‘sterilization’ of ACE acts, as a rule, on companies making investments capable of generating the multiplication of the benefit, while the relevance of the contribution is maintained for the receiving company, except in cases referred to in point 4, where the ‘sterilization’ reduces the increases in equity of the companies receiving the contributions.

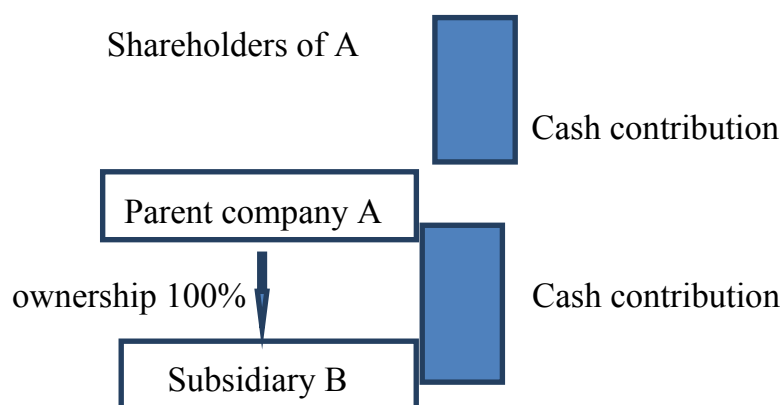
The Ace base ‘sterilizations’ envisaged for the intra-group transactions listed in the previous points may be disregarded if the taxpayer proves, even by submitting an advance ruling to the tax authority, that the increase in equity qualifying for ACE has not resulted in a duplication of the benefit within the group.

Cash contributions made in favour of residents

Cash contributions include also unconditional waivers by shareholders to the right to repayment of loans to the company or the offsetting of loans at the time of subscription of nominal capital increases, as well as the conversion of bonds into shares. The amounts resulting from the conversion of a debenture loan are equivalent, according to Circular No 12/2014 of *Agenzia delle entrate (Italian Revenue Agency)*, to a contribution in cash with the consequence that, if such amounts were transferred to other entities within the group through transactions referred to in the anti-avoidance provisions, a duplication of the ACE benefit might occur.

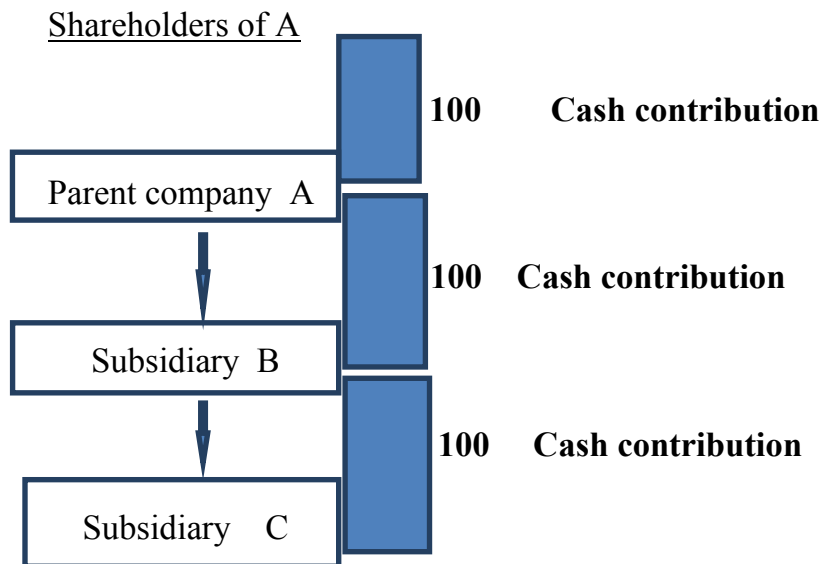
Let us consider, for instance, a group consisting of an Italian parent company that wholly controls a company that is resident in Italy¹ as well. If the parent company qualifies for ACE owing to the increase in equity following the listing of its shares on the stock exchange and subsequently makes a contribution in favour of the controlled company, the same parent company will have to ‘sterilize’ the ACE base for an amount equal to the cash contribution made to the controlled company.

In this event, with respect to the transferor parent company we already have here a case of cash contributions *"from any person"*, although not belonging to the same group market).



¹ Cf. Circular No 21/2015 of *Agenzia delle entrate*.

Another example occurs when a parent company A receives a contribution of 100 and with the cash received it makes a contribution of 100 to its controlled company B. In its turn, B makes a contribution to controlled company C for the same amount.

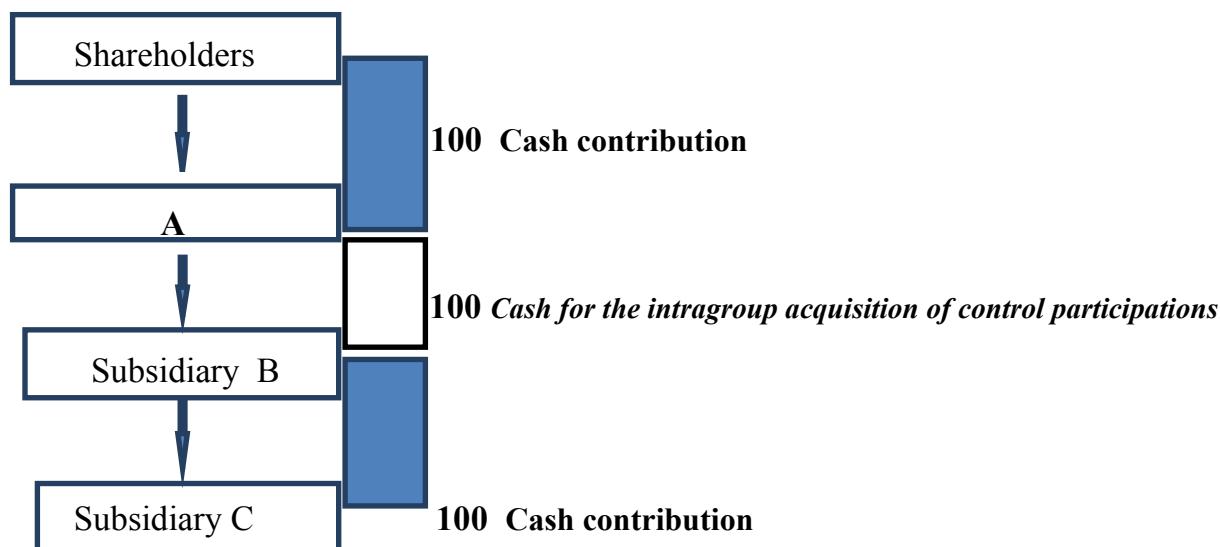


Parent company A will have an ACE base equal to zero since, against an ACE increase of 100 for the contribution received, it will have a decrease of 100 for the contribution made to subsidiary B. Also company B will have an ACE base equal to zero for the same reasons as parent company A. Subsidiary C will have an ACE base increase of 100.

Acquisitions or increments of control participations

Article 10(3)(a) of the ACE Decree requires the ‘sterilization’ of the increase in equity made in an amount equal to the sums paid for the intra-group acquisition (or increment of the participation held) of the equity investments in controlled companies.

Let us consider, for instance, the case in which company A receives a contribution of 100 and purchases control participations of 100 in enterprises from its controlled company B. With the cash received, company B makes a contribution to controlled company C for the same amount.



Focusing on company A, it will have an increase in the ACE base equal to zero (increase of 100 for contribution received and decrease of 100 for purchase of intra-group shareholdings). Company C will have an ACE base of 100.

Acquisitions of business or part of a business

Article 10(3)(b) of the ACE Decree requires the sterilization of the increase in equity made in an amount equal to the sums paid for the acquisitions of business or part of a business.

Also in this case, the scope of application of the legislation at issue is limited to intra-group purchases.

Cash contributions from: a) entities resident in countries which allow the exchange of information for tax purposes if controlled by resident entities b) entities resident in countries which do not allow such exchange of information

Article 10(3)(c) of the ACE Decree sterilizes, in the hands of the resident transferee, the cash contributions from non residents, belonging to the same group of the transferee in countries that guarantee the exchange of information, if controlled by residents.

The above-mentioned provisions sterilize the contributions received by the resident transferee whenever there is a risk – either real or potential – that the contribution may have been conveyed by a resident parent company to a non-resident entity.

In the cases of cash contributions from entities resident in so called “non-cooperative” countries or territories (i.e. tax havens, such as jurisdictions that do not guarantee the tax information exchange), the sterilization of the ACE base in the hands of the transferee, provided for by letter d), paragraph 3 of the above Article, applies instead also even when the non-cooperative transferor does not fall within the group to which the transferee (resident in Italy) belongs.

The first case occurs, for instance, when there is a group consisting of an Italian parent company that wholly controls a company resident in a cooperative country, which in turn totally controls a company also resident in Italy. If the non-resident company makes a cash contribution in favour of the Italian subsidiary, the anti-avoidance provisions apply through sterilization, for an amount equal to the cash contribution received, in the hands of the transferee entity.

A simple case of sterilization of contributions from residents in non-cooperative countries occurs, for instance, when a foreign company resident in such countries makes a cash contribution in favour of a company resident in Italy, which is 100% controlled.

In the case of group structures with multiple levels, both in Italy and abroad, the phrase “*from non-residents (...)*” contained in the ACE Decree implies an attitude – in order to apply the ACE anti-avoidance provisions – aimed at identifying the actual parent company of the foreign transferor (so-called *look through approach*).

Increase in financial credit for entities conducting activities other than banking and financial activities

Article 10(3)(e) of the ACE Decree provides that the ACE base variation has no effect up to the increase, vis-à-vis the increases resulting from the financial statements for the year ending on 31 December 2010, in financial credits to entities belonging to the group. Credits can be a suitable tool to multiply the ACE base when the company receiving the cash contribution lends the cash received to other companies for them, in turn, to make cash contributions conducive to generate further ACE base. The intention of the legislator was in fact to prevent that the same transferred amount of money could increase the equity of several legal entities belonging to the same group of companies.

Legislation amendments

The 2017 Budget Law has introduced some anti-avoidance provisions that limit the utilization of ACE.

In particular, the 2017 Budget Law extended the limitation provided for the carrying forward of tax losses and non-deductible interest expenses to the carry forward of ACE.

The ACE amount is compulsorily offset by the annual income of the taxpayer.

The excess of ACE amount (after the compulsory offset) cannot be carried forward in the case of (i) both a change of control and a change of the main business activity; or (ii) domestic and cross-border merger and demerger transactions.

The excess of ACE amount can no longer be carried forward to the following years where the company undertakes both a change (also temporary) of control and a change in its actual business purpose in the fiscal year in which the change of control arises or in the 2 preceding or following fiscal years, unless certain conditions are met. Correspondingly, in the case of mergers and divisions, the carry-forward of the excess of notional yield is currently limited to an amount not exceeding the net asset value resulting from either the last financial statements or the financial statements that must be prepared in the context of the merger or division, whichever is lower, without taking into account the increases made in the previous 24 months and subject to the condition that the profit and loss account shows an amount of revenue and labour costs exceeding 40% of the average of these items for the 2 previous fiscal years.

The limitation provided for the carrying of ACE excess may be disregarded if the taxpayer proves, even by submitting an advance ruling to the tax authority, that in that particular case any avoidance effect could not occur.