



FONDAZIONE
MAISTO

IFA

Interest on equity and debt, limitations on interest deductibility at national and international level

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Overview

- Deductibility limitations for Interest Expenses
- Challenges relating to Interest Deduction
- Italian Allowance for Economic Growth (ACE) regime
- Italian ACE vs. Debt-Equity Bias Reduction Allowance (DEBRA) Directive proposal

Deductibility limitations for Interest Expenses (1/2)

- **Opt-out** for the:
 - De minimis threshold
 - Standalone clause
 - Equity escape clause
 - Group ratio rule
- **Carry-forward mechanisms** are envisaged for the excess of: (i) net interest expenses over the 30% tax EBITDA threshold, (ii) net interest income, and (iii) 30% of the tax EBITDA (carry-forward limited to 5 years)
- Specific **ordering rules** govern how interest should be offset
- Specific provisions apply in case of **nationwide fiscal units**
- **Carve-outs:**
 - Financial undertakings
 - Loans for LT public infrastructure projects

Deductibility limitations for Interest Expenses (2/2)

- ❑ **Domestic SAARs**
 - Use of excess of net interest expenses under mergers and demergers subject to "vitality test"
 - Use of excess of net interest expenses denied if change of control and change of main business activity in given time interval
- ❑ **Transfer Pricing**
 - Possible loan recharacterization as equity injections
 - Free capital attribution to Italian PEs of foreign banks/insurance companies
- ❑ **Anti-hybrid mismatch rules**
- ❑ **Distressed companies, Insolvency and Debt Restructuring**
 - Interest expense carryforward forfeited in case of business turnaround

Challenges relating to Interest Deduction (1/2)

❑ Intragroup debt

- Interest mostly denied under Italian GAAR ([Ruling Reply No. 395 of 29 July 2022](#))
- Shareholder loans may be recharacterized as equity injections

❑ (M)LBO transactions

❑ Refinancing & cash repatriation

- Drawing down additional debt to refinance existing debt and/or to repatriate cash
- Repayment of IC loans vs. dividend distributions? (Impacts on interest deductibility, WHT tax risk, and NID...)

Italian Allowance for Economic Growth (ACE) regime

- Stock-incremental regime allowing **notional interest deduction**, determined by applying a deemed rate to the "net equity increase" as compared to the accounting net equity resulting on 31 December 2010
- Notions of "**qualifying equity increases**" and "**qualifying equity decreases**"
- **SAARs** setting out ACE base downward adjustments (unless a tax ruling application is filed)
- The adjusted ACE base is capped to the company's year-end accounting net equity
- Excess of ACE deduction may be **carried forward** (without time limitations, and usable also within fiscal units) or converted into a **tax credit** to offset IRAP (in 5 equal instalments)

Italian Ace vs. DEBRA proposal

- **Subjective scope** (re financial undertakings)
- Different **carry-forward** and **offsetting mechanisms**
- ACE vs. DEBRA **bases computation**
- Notion of **net equity increases**
- Relevance of **ex-ante stock capital**
- Impacts over **interest deductibility**

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THANK YOU!

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