

Real Estate Focus Team

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New interpretation of the tax-free step-up regime for taxpayers in the hotel and spa industry

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1. Introduction

Taxpayers in the hotel and spa industry may step-up the book and tax basis of assets in their financial statements as at 31 December 2019 without having to pay taxes (“**Tax-Free Step-Up**”)¹.

Italian tax authority (“**ITA**”) Circular No. 6 of 1 March 2022 (“**Circular**”) supersedes the ITA’s previous – and more restrictive – interpretation and significantly extends the Tax-Free Step-Up’s scope.

2. Main features of the option and the ITA’s previous (restrictive) interpretation

The Tax-Free Step-Up has the following main features:

- taxpayers can opt for it in relation to the 2020 or 2021 financial statements (for companies whose financial year coincides with the calendar year);
- it applies to all assets in a given “category”²;
- the stepped-up value is recognised for both accounting purposes and tax purposes, with no tax due³;
- the assets’ increased book value in the financial statements gives rise to a corresponding increase in the net equity. This increase qualifies as a ‘tax-deferred reserve’ (*riserva in sospensione d’imposta*), reductions of which generally trigger the application of ordinary corporate income tax⁴; and
- IAS/IFRS adopters cannot opt for the Tax-Free Step-Up.

¹ Art. 6-*bis* of Law Decree No. 23 of 8 April 2020, as converted into Law No. 40 of 5 June 2020.

² Based on clarification issued by the ITA for previous step-up options, the following “categories” apply to real estate assets: (a) building land with the same town-planning use; (b) non-building land; (c) non-commercial buildings; (d) commercial buildings ‘by nature’; and (e) commercial buildings ‘by use’.

³ When applied for tax purposes, the stepped-up value is recognised: (a) with no lock-up period for depreciation (higher tax depreciation can run from the year for which the Tax-Free Step-Up is requested); and (b) with a three-year lock-up period for capital gains (or losses) on the assets (e.g., in the case of disposal or assignment to shareholders).

⁴ The tax deferral can be avoided by paying a 10% substitute tax.

In addition to the Tax-Free Step-Up, taxpayers in the hotel and spa industry may opt for a tax-free ‘realignment’ of the tax basis of assets whose book value is higher than their tax basis⁵.

The Tax-Free Step-Up’s scope was unclear from the outset in many respects.

One of the main issues was whether owners of hotel assets leased to third parties could opt for the step-up.

A law provision⁶ expressly extended the application of the Tax-Free Step-Up to hotel assets leased out by the owner under a business or property lease agreement.

Notwithstanding the clear text of the new law, the ITA – in Ruling No. 450 of 30 June 2021 and the draft circular of 23 November 2021 – took the view that the Tax-Free Step-Up did not apply to companies that lease out hotel buildings but do not operate hotels/spas themselves⁷.

3. The new guidelines

This restrictive interpretation has now been superseded.

In fact, according to the Circular, the Tax-Free Step-Up applies to any taxpayer (even if it does not directly operate a hotel/spa) that:

- a. owns hotels or similar real estate assets; and
- b. leases these assets to taxpayers that operate (and employ these assets in) a hotel/spa⁸.

As the Tax-Free Step-Up is available also for FY 2021, the related deadline for opting in is still pending. To opt in, the step-up must be reported in the financial statements as at 31 December 2021, and **the option must be selected in the 2021 tax return (to be filed by the end of November 2022)**.

Given the ITA’s previous restrictive approach, hotel owners who leased out assets to hotel operators might have opted in 2021 for the alternative tax step-up regime, which – as opposed to the Tax-Free Step-Up – required the payment of a 3% substitute tax (“**Standard Tax Step-Up**”).

⁵ The “realignment” is applicable also to IAS/IFRS adopters.

⁶ Art. 5-*bis* of Law Decree No. 41 of 22 March 2021, converted into Law No. 40 of 5 June 2021.

⁷ The lone exception was for companies owning a hotel business (i.e., hotel building plus related business assets/going concern), if the business (including the real estate assets) was leased out under a business lease agreement/lease of going concern (*affitto di azienda*).

⁸ The Tax-Free Step-Up applies only to hotel buildings and, as a rule, cannot be extended to other corporate assets.

These taxpayers should thus evaluate whether it is in their interest to revoke their choice, request application of the Tax-Free Step-Up, and request a refund of the tax paid⁹.

Based on general principles, switching to the Tax-Free Step-Up would appear to be admissible, as the choice of the Standard Tax Step-Up was presumably biased by the ITA's restrictive (and now abandoned) interpretation. The actual feasibility of the approach – and the procedural steps to be taken – will have to be assessed on a case-by-case basis.



Real Estate Focus Team

The focus team is a constellation of skills in different practice areas with a focus on real estate.

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⁹ The Circular was issued on 1 March 2022, when the deadline for the 'ordinary' revocation of the Standard Tax Step-Up had already expired for taxpayers whose financial year coincides with the calendar year.