

||| Special Edition: 2020 Financial Statements

In brief

This note provides an analysis of the main provisions of various pieces of legislation passed to support businesses during the COVID-19 emergency, with specific regard to the preparation and approval of 2020 financial statements.

- || Revaluation of business assets
 - || Suspension of depreciation / amortization of fixed assets
 - || Option for exceptions to the provisions regarding the prospect of businesses continuing as going concerns
 - || Deferral of the terms for the approval of financial statements and "simplified" procedures for holding shareholders meetings
 - || Suspension of recapitalization obligations in the event of losses
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Details

Subject	Description
<p>Revaluation of business assets and realignment of values for tax purposes</p> <p>(Article 110, Decree-Law 104/2020, converted with modifications with Law 126/2020)</p>	<ul style="list-style-type: none"> With a view to encouraging capital injection and mitigating the consequences on financial statements of the economic crisis caused by the COVID-19 pandemic, the legislation has introduced the possibility of revaluing business assets in the financial statements for the year following the fiscal year in effect as at 31 December 2019 (and, that is, for companies with a fiscal year coinciding with the calendar year, revaluation in the 2020 financial statements). The revaluation can be effected by joint-stock companies, commercial entities, and persons having business income that do not adopt the international accounting principles (IAS/IFRS). The following assets can be revalued: tangible fixed assets, intangible fixed assets, and shareholdings entailing a controlling or significant interest as reported in the financial statements for the fiscal year in effect as at 31 December 2019 and still held at the end of the subsequent fiscal year. The legislation excludes the possibility of revaluation for: buildings and other assets whose production or trade is part of the business activity (so-called "commodities"). The revaluation can also concern a single asset, and it can be effected for statutory purposes only or also with a tax effect. To obtain recognition for tax purposes of the higher values resulting from the revaluation, the taxpayer must pay an alternative tax to corporate income tax (IRES), the regional tax on productive activity (IRAP), and any additional taxes. The rate of the alternative tax is 3%. The alternative tax can be paid in three, equal annual instalments, without interest, starting from 2021, and it is to be paid by the due date for the payment of the balance of income taxes. With regard to assets subject to depreciation or amortization, the revaluation can be done using one of the three methods provided by the Ministerial Decree 162/2001 and, namely: <ul style="list-style-type: none"> I through a proportional increase in the historical cost and accumulated depreciation / amortization, to keep the initial term of the depreciation / amortization period unchanged;



	<ul style="list-style-type: none"> I with an increase in the historical cost only, that is, with a reduction of the pre-existing balance of accumulated depreciation / amortization; I with a "mixed" method through an increase in cost and a reduction in the accumulated depreciation / amortization. II Should the revaluation also be done for tax purposes, the positive balance from revaluation is treated as a tax-exempt reserve subject to taxation in the event of distribution to shareholders. The taxpayer can partially or entirely eliminate the aforementioned possible taxation in the event of distribution and make the revaluation reserve freely distributable by paying an alternative tax of 10%. This alternative tax can be paid in three instalments according to the same terms provided for the alternative tax on the revaluation. II Should the 3% alternative tax be paid, the effects of the revaluation for tax purposes are: <ul style="list-style-type: none"> I as from 1 January 2021 as regards depreciation / amortization, the deduction limit for maintenance expenses pursuant to Article 102, Paragraph 7, Italian Consolidated Law on Income Taxes (TUIR), and the amounts of fixed assets instrumental for effecting the test on non-operating companies; I as from 1 January 2024 with regard to capital gains / losses in the event of sale, transfer for purposes unrelated to the company, and assignment. II The positive revaluation balance, which is the offsetting entry to the incremental value booked to the fixed assets, is to be reported in the financial statements: <ul style="list-style-type: none"> I in the event of revaluation for statutory purposes only, net of the deferred taxes computed on the mismatch between the value of the fixed assets for financial reporting purposes and the value of the fixed assets for tax purposes; I in the event of revaluation also for tax purposes, net of the 3% alternative tax. If the positive revaluation balance is not unencumbered by paying the 10% alternative tax, Italian accounting principle OIC 25 provides that deferred taxes must be recognized on the positive revaluation balance only if there are substantiated forecasts that this reserve is attributed to the shareholders, with consequent taxation of the company. II Special information regarding the following aspects will need to be reported in notes to the financial statements: <ul style="list-style-type: none"> I valuation criteria (Article 2427, Paragraph 1, n. 1, Civil Code); I statement of changes in the values of fixed assets (Article 2427, Paragraph 1, n. 2, Civil Code);
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	<ul style="list-style-type: none">I the nature and the use of the shareholders' equity accounts (Article 2427, Paragraph 7, n. 7-bis, Civil Code);I deferred tax assets and liabilities (Article 2427, Paragraph 1, n. 14, Civil Code).II The report on operations will need to indicate the following:<ul style="list-style-type: none">I the consistency of the values used for the purposes of the revaluation (Article 11, Paragraph 3, Law 342/2000);I the effect of revaluation on financial statement ratios (Article 2428, Paragraph 2, Civil Code).II The report of the statutory auditors and the report of the independent auditors with regard to the financial statements will need to indicate the criteria used for the revaluation and will need to certify that the revaluation is within the limits set by the law.II Even though not expressly required by the legislation, it is recommended that the revaluation be done based on a specific appraisal.II Finally, the revaluation must be recorded in the inventory records and in the register of assets subject to depreciation / amortization.II The legislation also provides for the possibility of realigning the values for tax purposes with the higher book values reported in the financial statements (so-called "realignment"). This option is applicable only on a tax basis, and it is also available to companies that adopt the international accounting principles (IAS/IFRS). The realignment is subject to an alternative tax of 3%, to be paid according to the procedures contemplated for the revaluation of the assets. Furthermore, considering the need to establish a tax exemption limitation on a shareholders' equity reserve equal to the value of the realignment, the taxpayer can eliminate the aforementioned limitation on the reserve by paying an alternative tax of 10%, according to the procedures and terms already described for freeing up the revaluation reserve. The deferral of the tax effects of the realignment is the same as that for revaluation (i.e. 2021 for depreciation / amortization and 2024 for capital gains / losses).
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Subject	Description
<p>Suspension of depreciation / amortization of fixed assets</p> <p>(Article 60, Paragraphs 7-bis-7-quinquies, Decree-Law 104/2020, converted with modifications by Law 126/2020)</p>	<ul style="list-style-type: none"> Entities that do not adopt the international accounting principles may elect not to take up to 100% of the annual depreciation / amortization of the cost of tangible / intangible fixed assets with reference to the 2020 financial statements. The suspension should be possible with reference to all fixed assets, standard categories of fixed assets, or individual assets. The percentage of depreciation / amortization not charged is to be recognized in the profit and loss statement of the following year, thereby extending the original depreciation / amortization period by one year. The entities who elect to suspend the charges must allocate to a restricted earnings reserve an amount that is equal to the portion of depreciation / amortization not taken. The notes to the financial statements must provide disclosures about the reasons for the exception, the recognition of the reserve, and the impact on the representation of the shareholders' equity, financial position, and the earnings results for the period. Regardless of its recognition in the income statement, the portion of depreciation / amortization suspended for statutory purposes can be deducted for tax purposes, within the limits set by the regulations for corporate income tax (IRES) and the regional tax on productive activity (IRAP). Such deduction leads to a mismatch between the value of the fixed assets for financial reporting purposes and the value of the fixed assets for tax purposes, and thus necessitates a provision for deferred tax liabilities.
<p>Exception to the provisions regarding the prospect of businesses continuing as going concerns</p> <p>(Art. 38-quater Decree-Law 34/2020)</p>	<ul style="list-style-type: none"> With reference to the preparation of the financial statements for the fiscal year in effect as at 31 December 2020, the legislation states that the valuation of the accounts and the assessment of prospect of a business continuing as a going concern (Article 2423-bis, Paragraph 1, no. 1, Civil Code) can be done on the basis of the results of the most recent financial statements for the fiscal year in effect as at 23 February 2020, i.e. the 2019 financial statements for companies whose fiscal year is the calendar year.



Subject	Description
<p style="text-align: center;">Deferral of the terms for approval of financial statements and "simplified" procedures for holding shareholders' meetings</p> <p style="text-align: center;">(Article 106 Paragraph 1 del Decree-Law 18/2020, as modified by Decree-Law 183/2020)</p>	<p>The legislation provides for:</p> <ul style="list-style-type: none"> an exception to the provisions of Article 2364, Paragraph 2 and Article 2478-bis, Civil Code, or other statutory provisions, so that the ordinary shareholders' meeting for the approval of the 2020 financial statements can be held within 180 days of the close of the year (i.e. by 29 June 2021, for entities with a calendar year as their fiscal year); the adoption of the simplifications contemplated by Article 106 of Decree-Law 18/2020 for all shareholders' meetings held until 31 July 2021; the simplifications allow for participation in the meetings through the use of telecommunications systems and equipment, provided that each participant can be properly identified, take part in the discussion, and cast their vote.
<p style="text-align: center;">Suspension of recapitalization obligations in the event of losses</p> <p style="text-align: center;">(Article 1, Paragraph 266 of Law 178/2020)</p>	<ul style="list-style-type: none"> The legislation establishes that the obligations provided by the Civil Code for joint-stock companies (S.p.A.) and limited-liability companies (S.r.l.) regarding capital reduction, recapitalization, and dissolution in the event of significant losses will not be applied to the losses accrued during the fiscal year in effect as at 31 December 2020. The legislation postpones, to the fifth subsequent year, the deadline within which the capital reduction and recapitalization measures must be adopted as well as the deadline from which the dissolution proceedings are applicable. More specifically, the following are postponed to the fifth subsequent year (i.e. approval of the 2025 financial statements): <ul style="list-style-type: none"> the deadline within which the loss must be reduced by at least one-third in the event of share capital reduction of more than one-third (Articles 2446 e 2482-bis, Civil Code); the deadline for the shareholders' meeting to resolve the capital reduction and the simultaneous capital increase to the legal minimum or the transformation of the company in the event of any reduction of share capital of more than one-third and to less than the legal minimum (Articles 2447 e 2482-ter, Civil Code); the dissolution proceedings for the company in the event of any reduction of the capital to less than the legal minimum (Article 2484, Paragraph 1, n. 4, Civil Code).



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| | <ul style="list-style-type: none"> The other provisions of the articles cited above remain unchanged. More specifically, the directors are nonetheless required:<ul style="list-style-type: none"> to oversee the occurrence of any significant losses during the year; to promptly convene a shareholders' meeting for the appropriate actions. The deferral of the recapitalization obligations also does not exempt the directors from their duties of proper management which require them to effect an assessment of the company's financial position and earnings, and to plan and implement measures aimed at restoring the earnings and financial balance. The following prohibition remains unchanged: If there is a loss of the share capital, there can be no distribution of profits or reserves until the capital is reinstated or reduced accordingly (Article 2433, Paragraph 3, Civil Code). The legislation provides that the losses recognized in the 2020 financial statements, whose coverage may be determined up to the fifth year thereafter, will be separately indicated in the notes to the financial statements, with specific disclosures about their origin and the changes occurring during the years. |
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