

# Italy and International Taxation

What a Foreign Investor Should Know

Transfer Pricing - Permanent Establishments - Black Lists

**June 18, ICC International Headquarters,  
Paris**



International Chamber of Commerce

*The world business organization*



**CRA** Charles River  
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# Tax Audits

- Can be conducted both by the Italian Tax Police and the Tax Agency
  - Tax Police: also for criminal investigations
  - Tax agency might anyway file a notice of crime with the criminal prosecutor
- Please note that Tax and Criminal trial are independent, and thus, in theory, **might lead to conflicting decisions (e.g., for the moment, KARNAK - a PE case)**
- Criminal proceedings are very important, though, also for Tax cases as
  - **Notice of crime allows extension of statute of limitations:**
    - Ordinarily it is 4 years (unfaithful tax return) or 5 years (omission to file the return)
    - In case a crime is (**allegedly**) detected: 8 or 10 years (double term)

# Relevance of criminal law, con'ed

- Since 2008 criminal conviction brings application of provisional seizure for the amount of taxes evaded (and finally to **confiscation**, if conviction or plea bargaining)
- This is **in addition to recovery of taxes and interest**.
- In such case, tax sanctions should normally be reimbursed (criminal sanction prevails under the *lex specialis derogat generali* criterion: art. 19, legislative decree 74/2000)
- However: criminal sanction is applied on individuals, while tax sanctions are on the company
  - **Pending decision** by the Supreme Court on the seizure applied to an Italian bank that entered an abusive scheme based on an int'l REPO transaction
- Current issues for the case law:
  - **Preposterous and instrumental use** by the Administration of the notice of crime for taking advantage of the longer statute of limitations
  - **Relevance of tax avoidance** for criminal law purposes
  - **Relevance of transfer pricing** for criminal law purposes
- The Government is also analyzing the issue and presented a **draft reform** (first draft rejected by the Italian President b/c no agreement on prospected full irrelevance of avoidance)

# Rights of the taxpayer during the

- Art. 12 of the Bill of taxpayers' rights (Law 212/2000)
- Audits to be conducted during ordinary business hours
  - Possibility to ask that analysis of docs be done at different location (lawyer/accountant's offices) so not to hamper business
- Right to express own views and arguments, to be recorded in the minutes of the audit and in the final report
- Duration: 30 days of *effective* presence at the business premises (with possible extension for additional 30 days)
  - It can therefore be much longer, and usually takes some months
- At the end of the audit: 60 days for the taxpayer to deposit its own **observations**
- Obligation for the Tax Agency to take them into account before issuing the reassessment notice
  - If they don't: possible annulment of the reassessment, as also in case of inaccurate consideration or in case the reassessment is released before the expiration of the 60 days period in absence of commanding reasons of emergency (Italian Const'l Court and Supreme Court)

- The results of the Audit Report might be:
  - accepted in full by the taxpayer (sanctions are then applied in the amount of **1/6 of the minimum**), or
  - refused in full (litigation starts, sanctions apply in full), or
  - Lead to the opening of a settlement procedure (accertamento con adesione)
    - Not exactly a negotiation, as it aims at a better determination of the actual income to be reassessed (Tax Administration cannot dispose of taxes due; it can only re-determine, together with the taxpayer and its counsel, whether something was actually due)
    - Difference with self-annulment (autotutela) by the Tax Agency:
      - Settlement procedure must bring to a redetermination of the income to be reassessed (if the parties finally do agree, otherwise litigation is still open)
      - Self-annulment is due when the tax claim is fully ungrounded (Regulation No. 37/1997):
        - » Mistakes on the identity of the taxpayer
        - » Mistakes of reasoning or calculation
        - » Mistakes on the taxable base
        - » Double taxation
        - » Taxes already paid
        - » Documentation at discharge subsequently (but still timely) provided by the TP
        - » Formal mistakes by the TP that could easily be detected by the Administration
      - Only limit: final decision by a judge

# Settlement procedure

- After notification of reassessment notice: **60 days to file appeal in tax court** (provincial tax court in first degree, regional tax court in second degree, Supreme Court for purely legal questions)
- **Extension of 90 additional days** if request for settlement procedure is filed
- Suspension of terms from August 1 to September 15
- In case of settlement: **sanctions reduced to 1/3 of minimum**
- Settlement still possible until first hearing in Tax Court: sanctions in this case reduced to **40 per cent**

# Provisional collection

- Distinction must be drawn between tax years up to 2006 and tax years from 2007 on, as in the first case the notification of an additional request of payment is needed
- In both cases: **provisional collection of 1/3** of the taxes and interest in case of appeal in tax court, **unless a freeze order** is granted by the tax court based on:
  - *fumus boni iuris*, and
  - *periculum in mora*
- In case of negative decision in first degree, **2/3** of the sums (inclusive of sanctions)
- In case of negative decision in second degree: **full payment** (reimbursable in case of victory before the Supreme Court)
- Non application of sanctions in case of compliant transfer pricing documentation)
  - ...incentive to litigate the case
  - Discounts on sanctions for repeated violations
    - Incentive to litigate in some cases (when extension of statute of limitations), provided amount of income finally reassessed is the same... which is not always granted and considering ongoing exposure to reassessment for the still auditable years



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# Trends for Tax Audits

- Circular letter 18/E of May 31 2012
- Focus will be on:
  - Aggressive tax planning (like REPO and stock lending arrangements)
  - Misuse of losses
  - International arbitrage
  - Transfer pricing and PE
  - Government itself makes clear they need money (page 29)
- Enhanced relationship (OECD standards)
- Audits starts based on risk analysis
  - No audit in last 4 years
  - Recurrent losses
  - Low income declared
  - Risk of VAT evasion (electronics and similar business sectors [risk of carousel frauds and then full audit on the whole sector just this year], Emission trading credits, cars, tyres etc.)

# Tax tutoring

- Tax Tutoring for the bigger taxpayers (revenue higher than 100 mio.)
  - audit within one year from filing of return
  - Risk analysis based on biz sector, track record of the TP, risk factor linked to the specific transactions
  - Additional audits to check compliance with rulings released for antiavoidance purposes
- Risk factors:
  - Int'l tax arbitrage
  - Reorgs
- Transfer pricing
  - P&L fluctuations
  - Rulings

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# MAP and convention 436/90/EEC

- OECD guidance strictly followed (in general, always true, and all the more so in the last years)
- Recently released circular letter No. 21/E of June 5 2012
- Competent authority: Ministry of Finance
  - Tax Agency for technical support on drafting of **position papers**
  - **Settlement** as well as **final decisions** impede MAP and 436/90/EEC
- **MAP art. 25 OECD Model convention (most times literally implemented in Italian double tax treaties)**
  - Optional and also **together with litigation** (always advisable to file the appeal anyway)
  - Only most recent DTCs contain binding arbitration clause, the most still providing for the signing States the obligation to start discussion and **endeavour** to eliminate double taxation (i.e., not to eliminate it)
  - Applies also to cases not covered by DTC (PEs of third country's companies)
  - Request to be filed with the Residence State as soon as double taxation arise (or is about to arise – flexible attitude by the Italian authorities on this: thus, also after a “mere” Audit Report): deadline is usually 2 years from the notification of the reassessment notice (3 years under some other conventions, e.g. ITA-SWI)
  - **Taxpayer must cooperate (by providing requested info and documentation)**
  - When litigation also pends, TP will have to finally communicate acceptance of int'l agreement or final reliance on the outcome of litigation
    - Tax Agency cannot override **final** decision of tax courts, so TP must decide before decision becomes final
    - If final decision by Italian judge against the TP, the only way to eliminate double taxation will be for the foreign tax authorities to “comply” with it
  - Litigation abroad is not impeditive to MAP, provided foreign authorities allow it
- Freeze orders against provisional collection can be granted either by the tax courts or by the administration itself

- Exchange of written position papers between the competent authorities and negotiation meetings; first to write is the State where double taxation arose
- Role of the TP: participation to provide explanations, comments and documents; right to be heard and to be informed
- **EEC convention 436**
  - Code of Conduct December 22 2009 is the basis
  - Request can be filed by resident TP or Italian Pes of foreign taxpayers (EU)
  - Exclusion of applicability in case of “serious” penalties: Italy would deny it only in case of tax frauds (in fact, it never happened)
  - Request to be filed within 3 years from the notification of the reassessment that gave rise to double taxation
  - Competent authorities have 2 years to solve the issue on mutual agreement basis; thereafter, appointment of advisory committee and arbitration procedure
    - Procedure ends with either:
      - Agreement within 2 years, or within 6 months after opinion of advisory committee, or
      - Expiration of 6 months from the release of the opinion by the advisory committee



# ...con'ed

- While obviously applies for determination of income attributable to a PE (Art. 7 OECD), not clear whether can be applied for undisclosed PEs (Art. 5)
- **Choice** must be made between arbitration and litigation before national courts, as the convention provides for the guarantee that double taxation will be eliminated (although not always in the sense wished by the TP), therefore arbitration only if:
  - No appeal (remedy against failure to timely appeal)
  - No final decision yet and TP gives up litigation
  - Litigation only limited to amount of penalties (disapplication of sanctions for good faith, etc.), not on taxes
- Italian judge always commands
- Freeze order by the Tax Agency itself can be granted (Art. 3.2 of the implementing law 99/1993); guarantees might be requested

# Rulings

- Ordinary ruling: clarification of legal interpretation of a given provision
  - Answer binds the administration (both for taxes and sanctions)
- Special ruling (anti-avoidance provisions)
  - Binds the administration only for sanctions
- International ruling (unilateral APA)
  - Binds for three years

# Most relevant issues for foreign investors

- Transfer pricing
  - Characterization of TP provisions as anti-avoidance (favorable for the TP)
  - Burden of the proof
    - Certification of balance sheet
  - Biz restructurings ...and tax neutrality: how do they reconcile? Role of exchange of information and int'l assistance in the collection of taxes
- Intangibles
  - Sponsorship of weather forecast *Epson Meteo* (Supreme Court 2012)
- PEs
  - Italian case law and experiences
    - *Philip Morris* (the [mis]leading case)
    - *Karnak* (art. 5 and 7 applied)
    - *Boston Scientific* (commissionaire arrangement: not a PE)
    - *Voith Paper*: who should be the addressee of the reassessment?!?
    - Risks of too powerful country managers
    - Careful drafting of employment agreements and other parent/subsidiary arrangements
    - Corporate communication: emails and their use in the audits and in court
    - Form and Substance in the performance of group functions/assumption of risks/use of assets
    - PoA and negotiation of discounts
    - Overview of execution of contracts on behalf of parent co.
    - Secondment of employees and PEs
    - Capital structure of PE (dotation fund needed, before interest expense deduction can take place: ruling No. 44/E 2006 and Tax Court of Milan 475/2010)
    - Dependent agent PEs and transfer pricing
      - Single taxpayer approach vs. AOA : OECD guidance (Report of 2008 on attribution of profits to PEs)
  - Most recent foreign case law
    - *Zimmer*
    - *Dell*
    - *Roche* (both for 5.1 and 5.4 OECD Model)

# Most relevant issues for foreign investors, con'ed

- Residence of subsidiaries subject to too strict a control by Italian resident holding/subholding (regional headquarters) Italian Supreme Court 7080/2012
- Black lists
  - CFC
    - Mix of jurisdictional (black list) and transactional (passive income) approach
    - Both for controlled and merely related companies (20 per cent of profit sharing, 10 if listed), although with different rules and in the former case only in case of black list companies
  - Denial of the deduction for costs and any negative item of income incurred toward a black list counterparty, unless:
    - Prove that counterparty really conducts business activity in the black list country, or
    - Prove that transaction was based on actual business needs and was effectively concluded
      - Approach of tax agency and case law is very strict: need to prove that no better conditions elsewhere (inclusive of costs of transportation and so on) and irrelevance of imposition of black list invoice by the counterparty
        - » Art. 24 of OECD Model stops this rule (Tax Court of Milan 338 of December 20<sup>th</sup> 2010)
- Arbitrage
  - OECD recent paper on Hybrid Mismatch Arrangements
- Re-characterizations
  - Debt vs. Equity (financial instruments/shares/bonds and loans/silent partnerships)

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# ... con'ed

- Corporate reorganizations
  - Tax neutrality
    - int'l mergers vs. liquidations
      - Taxation of latent gains (i.e., no neutrality), and
      - (informally) w/h taxation on outbound liquidation proceeds (likely to be against art. 5 of directive 435/90)
    - conversion of a branch into a subsidiary: tax treatment of the newly issued shares
    - Push down of debt for acquisition
      - LBOs (quite recent decision of Supreme Court: 1372/2011, in favor of TP)
    - Debt work-outs and windfall gains
    - Exit taxation, revised after ECJ *National Grid Indus BV*
      - Closure of a branch: a realization event according to ruling No. 124/E of 2006 (also refers to the client list and other intangibles)
      - ...and reverse: the recognition of tax values **at entry** into the Italian taxing jurisdiction (according to Tax Agency it depends on foreign exit taxation / critique / countermeasures / risks of reorgs)
- Beneficial ownership
  - Int'l standards (power to decide use of assets producing income or to dispose of income); risk factors: absence of entrepreneurial risk, scarce operative structure, single shareholder (Tax Court of Turin 14/2010 - and in a sense may be also the case of D&G, now in dispute before the Criminal Tribunal of Milan after a conviction in first degree before the Tax Court of Milan / interactions with abuse of law and transfer pricing rules and - since 2009 - also CFC rules)

# You can find more at

- [www.uckmar.com](http://www.uckmar.com)

- Blog with interviews to newspapers and other nation-wide comments of members of the firm and with the list of events we organize (mostly... conferences on tax law!)

- [www.studiouckmar.com](http://www.studiouckmar.com)

- Website of the firm

- [www.dpti.it](http://www.dpti.it)

- (the law review on int'l taxation that we run – I am the chief of the editorial staff)



# What you find in the folder

- Cover page of:
  - **Manual on Italian Int'l Taxation** 2012 edition
  - The three tax law reviews that we run (domestic taxation, int'l taxation and taxation of financial instruments)
- My most recent publication (*The Taxation of Dividends in Italy*, IBFD, 2012)
- A short CV with my publications





# Italy – Transfer Pricing Documentation Rules

June 2012

**CRA** Charles River  
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# Italy – Transfer Pricing Documentation Highlights

- Applicable to the tax year 2010 onwards
- Documentation not compulsory but highly recommended:
  - Provides protection from very heavy penalties
  - Its existence will be considered by Tax Authorities for risk assessment purposes
- Very rigid compulsory structure
- Detailed instruction published in December 2010 explicitly links the Italian rules to OECD Guidelines and EU Code of Conduct
- The taxpayer must notify to the Tax Administration the existence of transfer pricing documentation at the time of filing the tax return; can also cover older years by notifying before the start of an audit (still possible). Notification is a condition for penalty protection.
- Very short deadlines to deliver documentation:
  - 10 days
  - 7 days in case of supplemental requests

# Italy – Documentation Structure

- Compulsory content and structure, varying according to the nature of the local entity

Nature of the local entity	Documents required
(Italian) Holding	Master file and Country file (both in Italian)
Sub-Holding	Master file and Country file (MF can be in English)
Subsidiary (of a foreign Group)	Country file (in Italian)
Permanent Establishment	Depend on the head office structure

- Broadly follow the EU Code of Conduct, with some specificities:
  - Business strategies
  - Amounts and flow charts of transactions
  - Business rationales supporting the way intercompany flows are structured
  - Changes related to business restructurings

# Master File Content [1/6]

1. A general description of the multinational group (history, recent developments, business sectors in which it operates and overview of relevant markets of reference)
2. Multinational Group Structure
  - 2.1 Organizational Structure [including an organization chart, a list of group members, their legal nature, including reference to their shareholding percentages]
  - 2.2 Operational Structure [This paragraph contains a general description of the role that each of the associated enterprises carries out with respect to the multinational group's activities.]
3. Business strategies pursued by the Multinational Group, [with specific reference to its development and consolidations strategies] including potential changes to the overall business strategies if compared to the previous tax year

## Master File Content [2/6]

4. Transaction flows [In this paragraph, an overview of the general transaction flows as described in the following Chapter 5 must be provided for, including the invoicing flows and the amounts thereof and describing the underlying legal and economic reasons on the basis of which the activity has been structured as shown in the transaction flows. The transaction flows will have to be described in a flow chart encompassing also those pertaining transactions not falling into the ordinary management activity.]

# Master File Content [3/6]

## 5. Intra-Group Transactions

5.1 Sale of tangible or intangible assets, provision of services, financial services transactions [Each of the following paragraphs shall provide, for each set of transactions: (i) a description of the underlying nature of the intragroup transactions, with the option of excluding those involving transfer of goods or services between associated enterprises both resident for tax purposes in countries other than the European Union; and (ii) a list of the entities part of the multinational group, between those indicated in the previous Chapter 2, amongst which the transactions involving the above described goods and services were carried out. Similar categories of goods and services may be aggregated in accordance with the guidance provided for by the OECD Transfer Pricing Guidelines.]

5.1.1 Transactions type 1

5.1.2 Transactions type 2

5.1.n Transactions type n

# Master File Content [4/6]

5.2 Intra-Group Services [Each of the following paragraphs shall provide in detail the features of intra-group services carried out by one or more associated enterprises to the benefit of one or other associated enterprises and the entities part of the multinational group, between those listed at Chapter 2, between which the said services are carried out.]

5.2.1 Services type 1

5.2.2 Services type 2

5.2.n. Services type n

5.3 Cost contribution arrangements [In this chapter, a list regarding the actual cost contribution arrangements shall be provided, with an indication, for each arrangements, of the scope, duration, members of the arrangement, areas of activity and projects covered.]

# Master File Content [5/6]

6. Functions performed, assets used and risks assumed [In this chapter, the taxpayer will have to provide a general description of the functions performed, assets used and risks assumed by each of the enterprises involved in the transactions and of potential changes occurring in the functions, assets and risks if compared to the prior taxable year, with specific reference to changes triggered by business restructuring transactions.]
7. Intangible assets [in this chapter, a list of the intangible assets owned by each associated enterprise will have to be provided for, with a separate identification of any royalty payment, separated per recipient or payer respectively, and paid as a result of the exploitation of them.]



# Master File Content [6/6]

8. Transfer Pricing policy of the Multinational Group [In this chapter, a description of the multinational group's transfer pricing policy will have to be provided for, and of the underlying rationale that should support its consistency with the arm's length principle. In order to substantiate this information, it will be necessary to briefly refer to the contractual arrangements underlying the above mentioned transfer pricing policy.]
9. Relationships with the tax administrations of the Member States of the European Union regarding the Advance Pricing Arrangements (APAs) and transfer pricing rulings [In this paragraph, a brief description of the APAs and rulings signed by or released from the tax administrations of the countries in which the multinational group operates will have to be submitted, by describing the scope, content and duration of each agreements. The paragraph should be structured per country.]

# Country Specific Documentation Content [1/6]

1. General description of the enterprise (history, recent evolution and general overview of the relevant markets of reference)
2. Business Sectors
  1. Sector 1
  2. Sector 2
  3. Sector n
3. Enterprise's organization chart [The paragraph contains a general overview of the role that each of the enterprise's business units carries out within the general activity.]
4. General business strategies pursued by the enterprise and potential changes compared to the previous tax year's [The paragraph contains information regarding also specific strategies on specific sectors or markets.]

## Country Specific Documentation Content [2/6]

5. Controlled transactions (sale of tangible or intangible goods, provision of services, financial services transactions) [The current chapter can be divided in a number of paragraphs (from 5.1. to 5.n and corresponding subparagraphs) corresponding to the different type of transactions carried out between members of the multinational group. Consistent categories of transactions may be aggregated in a manner consistent to the guidance endorsed by the OECD Transfer Pricing Guidelines. In each of these paragraphs, the nature of transactions involving goods and/or services above mentioned will have to be described in detail, including the intra-group services. In the introductory part of the chapter, a list of the transactions described in the following paragraphs together with a detailed chart of the transactions' flows have to be submitted, including the amounts, describing the underlying economic and legal reasons on the basis of which the activity has been structured as described in the flow chart.]

# Country Specific Documentation Content [3/6]

## 5.1 Type 1 transactions

5.1.1 Description of the transactions [This section shall also indicate a list of the group members counterpart in the transactions. It will have to be expressly mentioned the circumstance whereby the same or similar transactions have been taking place between independent parties.]

## 5.1.2 Comparability analysis

- Characteristics of property or services
- Analysis of the functions performed, risks assumed and assets used [In this section, an indication of potential changes in the functions performed, assets used and risks assumed compared to the previous tax year will have to be provided for, with specific reference to changes if occurred in the context of a business restructuring.]
- Contractual terms [This section requires to report the key elements of written contracts regarding the transactions, specifying if they have general validity among the group.]
- Economic circumstances [This section shall contain references to the general features of the relevant markets, irrespective if they are relevant for supply, transit or distribution.]
- Business strategies

# Country Specific Documentation Content [4/6]

## 5.1.3 Selection of the transfer pricing method

- Description of the selected transfer pricing method and of the underlying reasons determining its consistency with the arm's length principle [This section shall also report the outcome of the comparability analysis that has determined the selection of the transfer pricing method deemed to be the most appropriate to the circumstances of the case. Should a transactional profit method be selected when a traditional transactional method could be applied in an equally reliable manner, it should be explained why the latter had been excluded. The same explanation applies in case of a selection of a method other than the CUP method, in the event the latter could potentially be chosen by the taxpayer.]
- Criteria for the application of the selected transfer pricing method [Within this section, an accurate description of the procedure followed by the taxpayer for the selection of comparable transactions will have to be provided for and, if needed, a clear description of the underlying reasons for identifying a specific arm's-length range.]
- Results deriving from the application of the selected transfer pricing method

5.n Type n transactions [Additional paragraphs and following subparagraphs at 5.1., if needed, will have to be structured according to the above mentioned scheme.]

# Country Specific Documentation Content [5/6]

## 6. Intra-Group Transactions (Cost Contribution Arrangements or “CCAs” to which the enterprise is part of)

- 6.1 Participants, scope and terms
- 6.2 Activities’ framework and projects covered
- 6.3 Method used for the determination of the expected benefits for each participant, including expected results, partial outcomes and divergences
- 6.4 Form and amount of each participant’s contribution to the arrangement, including methods and criteria to determine them accordingly
- 6.5 Formalities, procedures and consequences arising from the entry and withdrawal from the CCA by associated enterprises participating to it, including the termination thereof
- 6.6 Contractual arrangements concerning balancing payments or amendments to the CCA stemming from a change of circumstances
- 6.7 Changes occurred during the validity period of the CCA

# Country Specific Documentation Content [6/6]

- ANNEX 1 – Flow chart describing the transaction flows, including those falling out of the scope of the ordinary management activities
- ANNEX 2 – Copy of written contracts on the basis of which the transactions referred to at Chapters 5 and 6 are regulated

# Conclusion – Main Concerns

- Potential formalistic approach
- Rigidity of the structure
- Workload
- Language
- Consistency with other countries
- Very short time allowed to answer additional requests





# Italy – Tax Audit Directions - 2012

June 2012

**CRA** Charles River  
Associates

# Instruction Issued by the Italian Revenue Agency

- Administrative instruction (Circ.18/E) published on May 31, 2012
- Subject: “Preventing and fighting tax evasion – year 2012 – operational guidelines”
- Addressed to all Regional and Local offices, copying the Ministry of Finance, the Central Government Directorates and the Tax Police (Guardia di Finanza).
- 30 pages

# Circ.18/E - Content

## 1. Forewords

## 2. Specific Activities

1. Large taxpayers
2. Medium size enterprises
3. Small companies and self-employed workers
4. Non-commercial entities, subsidized entities
5. Individual taxpayers

## 3. Cross Activities

1. Anti-fraud activities
2. Activities against international tax evasion
3. Activities with international dimension
4. Activities related to indirect taxes (excluding VAT)
5. Collection activities

## 4. Planning and Reporting

## 5. Target Amounts for 2012

# Circ.18/E – 1. Forewords

- Improved results in 2011 in terms of quality and of increased amounts assessed
- 2012 targets are set at levels similar to 2011 results
- Focus on risk assessment and efficient use of resources
- Focus on cases of recurring tax evasion:
  - Non declared income (by companies or self-employed taxpayers), which typically impacts also the VAT income
  - VAT compliance
  - Under-declared income of individual taxpayers
- In addition to the targets already defined, the Management of the Revenue Offices will be measured also on the improvements in the above focus areas

## Circ.18/E – 2.1. Large Taxpayers

Year	Nr. of assessments	Additional taxes assessed – M €	Avg.additional taxes assessed - M €
2009	1,667	3,027	1.8
2010	2,609	5,490	2.1
2011	2,763	5,532	2.0

- Factors contributing to the results:
  - Professional development of audit resources
  - Quality of settlement negotiations
  - Coordination with foreign Tax Administrations in particular in sharing experience about fighting aggressive tax planning schemes
  - Improved interaction with taxpayers (in particular within “Tutorship”)
  - Significant synergies with the Tax Police
  - National joint committee between the Tax Administration and the Tax Police to address complex and highly relevant issues

# Circ.18/E – 2.1. Large Taxpayers

## TUTORSHIP

- Expanded in 2012 to all large enterprises (3,200 entities – Revenue > 100 M in 2010)
- Focus on risk assessment
- Focus on aggressive tax planning schemes:
  - Corporate loss utilization
  - Hybrid mismatch arrangements
  - Transfer Pricing (focus on documentation)
- Risk assessment formalized process / forms / tools
- “Enhanced relationships” approach:
  - Taxpayer proactiveness as an element of rating the risk
- Audit activities focused mainly on 2009 and also 2010

## Circ.18/E – 2.2. Medium Size Enterprises

Year	Nr. of assessments	Additional taxes assessed – M €	Average additional taxes assessed - K €	Median additional taxes assessed – K €
2009	12,008	4,600	384	n.a.
2010	15,524	6,300	405	24.5
2011	16,080	7,700	478	34.0

- Good results, but this segment is still considered an area of significant tax evasion/avoidance
- Additional initiatives envisaged:
  - Regional Offices to supervise the risk analysis, in particular for the medium-large segment (companies with revenue > 25M €)
  - Support of skilled resources to Local Offices
  - Transfer of complex enquiries to Regional Offices
  - Higher coordination with the Tax police

## Circ.18/E – 2.2. Medium Size Enterprises

- Audit activities will be prioritized on the basis of the following main risk factors:
  - Lack of audits in the last four years
  - Recurring losses
  - At least two years with income significantly lower than the average in the business sector
  - Risk of VAT evasion
- Audit activities focused mainly on 2009 and also 2010
- Overall target reduced for 2012, but increased target for the median assessment, focusing in particular on VAT.



## **Circ.18/E – 3.3. Activities with International Dimension**

Activities requiring further development:

- Exchange of information (in particular on VAT)
- Simultaneous audits (Fiscalis)
- International ruling (unilateral APA)
- Intra-community VAT
- International collection activities
- Double taxation issues (separate instruction published)
- MAP dedicated resources



# Italy – International Standard Ruling

June 2012

**CRA** Charles River  
Associates

# The “International Standard Ruling”

- Entered into force in 2004, operational since 2005.
- Not a unilateral decision of the tax administration; agreement between the taxpayer and the tax authority.
- Equivalent to a unilateral APA.
- Since the beginning aimed at:
  - improving cooperation and dialogue between taxpayers and the tax administration; and
  - providing legal certainty to both of the parties, preventing legal disputes and reducing the risk of international double taxation.
- Instruction letter dated April 2010 summarizes rules and actual experience.

# Applicable Matters

- The correct transfer pricing methodology applicable to the transactions carried out with related parties.
- The tax treatment provided for by law, including tax treaties, in respect of dividends, interest, royalties or other income paid to or received from non-resident persons in specific cases.
- The application of the provisions of the law, including tax treaties, to specific cases related with the attribution of profits or losses to permanent establishments in Italy of non-resident enterprises as well as to permanent establishments abroad of resident enterprises.

# Process

- Two national offices in charge of all rulings:
  - Rome (Center and South of Italy)
  - Milan (North of Italy)
- The 2010 instruction letter provides details about the content and form of the ruling requests.
- Procedure based on meetings and discussions with the taxpayer.
- Non-binding term of 180 days to complete the process.
- Completed by signing an agreement binding both parties.
- In force for three years starting from the tax period of signature.
- Renewable.
- Agreed monitoring process to verify correct implementation.

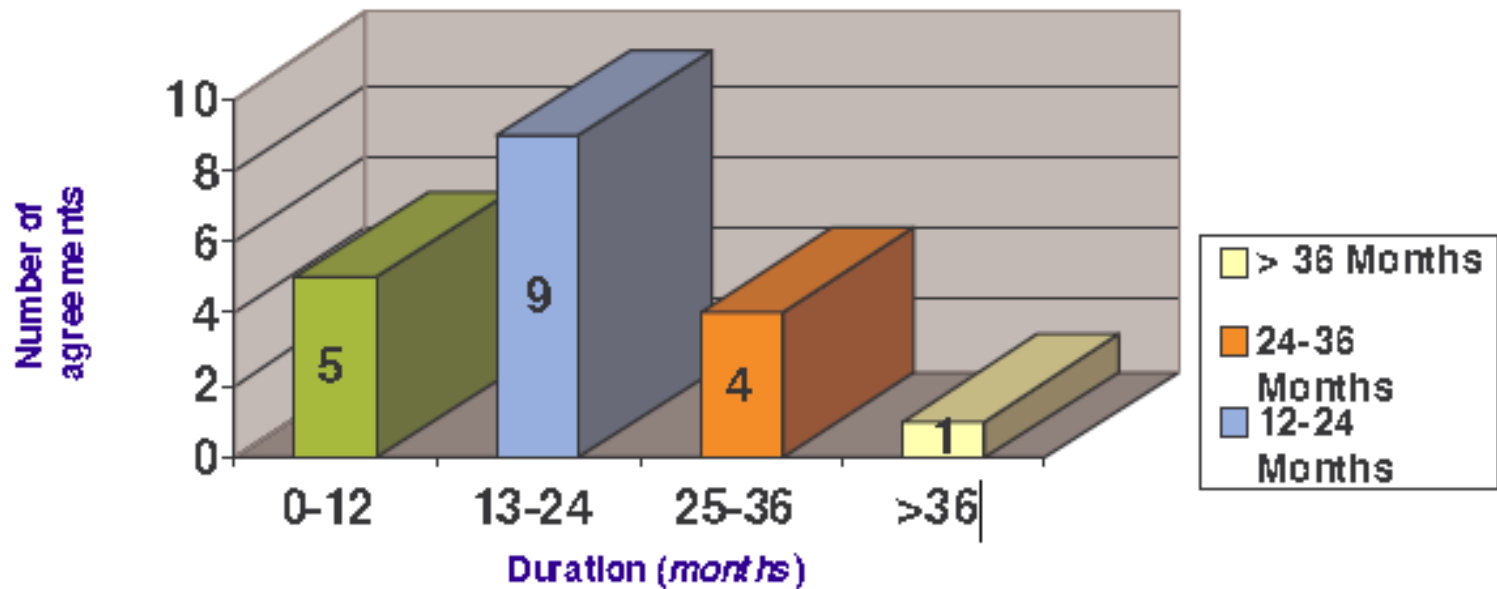
## 2004-2009 Results

### Applications for international standard rulings submitted during the period 2004-2009

	<i>Total</i>
<i>Applications submitted</i>	52
<i>International rulings granted</i>	19
<i>Procedures in progress</i>	17
<i>Applications rejected</i>	7
<i>Applications withdrawn</i>	9

# 2004-2009 Results

GRAPH 2 – Percentage share of international ruling agreements by class of duration  
(months)



# 2004-2009 Results

<b>Methods used for determining transfer prices</b>		
<b>Description of methods</b>	<b>No. cases</b>	
	<b>Partial</b>	<b>Total</b>
<b>Comparable Uncontrolled Method (CUP)</b>		<b>1</b>
Internal comparables	1	
External comparables		
<b>Cost Plus Method (CPM)</b>		<b>3</b>
Internal comparables	2	
External comparables	1	
<b>Resale Price Method (RPM)</b>		
Internal comparables		
External comparables		
<b>Transactional Net Margin Method (TNMM)</b>		<b>10</b>
PLI (profit level indicator): mark-up on total costs	7	
PLI (profit level indicator): return on sales	3	
<b>Profit Split</b>		<b>5</b>
Contribution analysis		
Residual analysis	5	
<b>Total*</b>		<b>19</b>



# 2004-2009 Results

Cases of transactions in the agreements signed	
Cases of transactions	Number of transactions in the agreements signed*
<i>Sale of tangible property into Italy</i>	11
<i>Purchase of foreign goods</i>	4
<i>Performance of services by Italian entity</i>	3
<i>Performance of services by non-Italian entity</i>	0
<i>Cost sharing agreements</i>	1
<i>Transactions involving intangible property</i>	1
<i>Attribution of profits or losses to a permanent establishment</i>	2

\* The total number of agreements given in the current table does not coincide with the number of “Ruling agreements concluded during the 2004-2009 period”, since an agreement may also include more than one kind of transactions between related parties



# Italy Transfer Pricing

June 2012

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# Specific Provisions in the Italian Consolidated Income Tax Act

- Art. 9: Defines the concept of “Normal Value”: Price of similar goods and services, between independent parties, at the same level of trade, time, location (or the closest possible). Reference is also made to list prices, tariffs and regulated prices.
- Art. 110(7): Intercompany transaction shall be valued according to the normal value of the goods transferred or of the services rendered and received.

# Administrative Instructions

- An instruction letter of 1980, still formally in place provides detailed guidance on the application of the arm's-length principle.
- The instruction letter on documentation of December 2010 provides a background of the applicable rules, making explicit reference to the 2010 version of the OECD Transfer Pricing Guidelines and to the EU Code of Conduct.

# Practical Aspects of Transfer Pricing Audits

- Adherence to OECD guidelines (but practical approach of auditors may vary, based on their skill)
- Audits conducted by the Tax Police or the Tax Office
- Transfer Pricing methods
  - Traditional Transactional Methods
  - TNMM
  - Profit Split
- Peculiarities of use of comparables
- Frequent focus on intercompany services
- Role of documentation
- Links with permanent establishment issues
- Formal aspects require careful handling

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