FYI GGi GLOBAL ALLIANCE

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Italy

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ITALY

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Overview

Italy, as a member country of the OECD, has adopted rules inspired by the OECD Transfer Pricing Guidelines. Consequently, the transfer pricing methods accepted by the Italian Tax Authority (ITA) are the same as those outlined by OECD (i.e. comparable uncontrolled price (CUP), cost plus, resale price, transactional net margin, and profit split methods).

Only where one of the OECD transfer pricing methods is not applicable, may the taxpayer adopt a different method. On the other hand, where the taxpayer has selected one of the OECD methods and proved it is the most appropriate to the circumstances of the case, ITA is bound to use that method.

As to the arm's length prices that ITA considers to be in accordance with the arm's length principle, only recently has the full range of arm's length values been recognised as fully compliant, whereas in the past it was common practice to raise objections when the price charged in intercompany transactions deviated from the median value.

Reporting requirements

Apart from the preparation of the transfer pricing documentation, which is **optional**, reporting requirements imposed on Italian taxpayers are very limited.

In the tax return it is **mandatory to disclose the amount of cross-border, intragroup transactions** (income and expenses) without further reference to the transfer pricing methods selected.

It is also necessary to indicate whether the TP document has been **prepared for the**

financial year to which the tax return relates.

TP documentation

While all Italian taxpayers engaging in cross-border transactions with related parties must comply with the OECD arm's length principle, **the preparation of TP documentation remains a mere option**.

However, if prepared on time and in compliance with domestic regulations, **TP documentation guarantees the so-called penalty protection** – in the event of transfer pricing adjustments, **no penalties will be imposed**.

Penalties from transfer pricing adjustment range from **a minimum of 90% to a maximum of 180% of the additional income tax** deriving from the adjustment.

Given the very heavy penalties imposed, preparing TP documentation is absolutely appropriate for medium sized or large multinationals, where even a small TP adjustment can result in a significant number of penalties.

TP documentation consists of a **master file** and a **country file,** whose structure and contents are set out by domestic regulations and are consistent with the OECD Guidelines.

It is interesting to note that as of the financial year 2020, **the master file could**

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be prepared in English, thus allowing Italian subsidiaries of multinational groups to use any documentation prepared by the group's headquarters.

In contrast, the **country file** must be prepared exclusively in **Italian**.

Deadline to prepare TP documentation

To guarantee the penalty protection, **TP Documentation must be prepared by the deadline for e-filing the annual tax return**, i.e. the last day of the eleventh month following the end of the financial year.

Therefore, for taxpayers who adopt the calendar year – the vast majority in Italy – this deadline is 30 November.

By this date, the TP documentation must be digitally signed by the legal representative of the taxpayer and a **time stamp must be affixed** to certify the timeliness of the documentation. Failure to affix the time stamp will not allow the taxpayer to benefit from penalty protection.

The TP documentation must be delivered to the Italian Revenue Agency within 20 days of the relevant request, whereas if during a tax audit a taxpayer is required to provide additional or supplementary information, it must be provided within 7 days.

Practical tips for a TP audit

As mentioned, **TP documentation (master file and national document) is the best protection tool during a tax audit**, especially for those taxpayers with a significant amount of intragroup cross-border transactions.

It is very important that TP documentation clearly sets out the steps taken in performing the TP analysis, and focuses on how the comparable taxpayers were selected and the "arm's length range" of comparable prices was built, considering that:

- ITA uses the same TP databases as those used by taxpayers, and therefore can easily replicate any TP analysis run;
- The statute of limitations in Italy is 6 years, so it is very likely that the set of information (i.e. financial statements of comparable taxpayers) available to ITA at the time of the audit is much more extensive than that used by the taxpayer at the time of the analysis; and
- While ITA usually accepts the transfer pricing method selected by taxpayers who prepare the TP documentation, it very often adjusts the analysis performed by them, for example, by excluding some of the comparable taxpayers selected or adding new ones.

Advanced pricing agreements (APAs), dispute avoidance and resolution

With a view to preventing litigation, **Italian taxpayers have access to APAs** – though they are still not very widespread and are confined to large companies, because of the time required to reach an agreement and the complexity of the process.

APAs are binding for ITA for a total period of **five fiscal years**; the one in which the agreement is signed and the four subsequent years.

If, on the other hand, a taxpayer suffers a transfer pricing adjustment, a settlement with ITA can be reached. In this case, **penalties are reduced to 1/3 of the minimum** unless penalty protection is applicable.

Moreover, the Italian government recently introduced **a simplified procedure for the recognition of correlative adjustments, which gives Italian taxpayers the opportunity to reduce their taxable income** where, for example, a foreign related party suffers a transfer pricing adjustment relating to a transaction in which an Italian taxpayer is the counterparty. The latter may ask ITA, under certain conditions, to reduce its taxable income, mirroring the adjustment suffered by the foreign related party.

The simplified procedure will lead to an agreement within a relatively short period of time (180 days).

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