



Transfer Pricing
Country Summary

Italy

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1. Introduction

Italy is a member state of the OECD. It has adopted the transfer pricing documentation requirements resulting from BEPS Action 13 into its legal framework. Meaning that local file, master file and CBCR reporting are included in the legislative framework. However, these transfer pricing criteria remain optional, as they were previously: MNEs may choose to prepare a transfer pricing paperwork on their yearly corporate income tax returns in order to be protected by the Italian penalty protection framework.

2. Laws & Regulations

a) References to OECD/EU/Local Rules

Transfer pricing legislation is laid down in Article 110, paragraph 7 of the Italian Income Tax Act, expressly referring to the arm's length principle that is set forth by Article 9 of the OECD Guidelines. The principle is strengthened later on by the Ministerial Decree of 14 May 2018 in Article 1 directly referencing to term.

b) Definition of Related Party

The amended (in 2017) version of Income Tax Code in Art. 110 par. 7, refers to transactions carried out between Italian companies and non-resident companies. The article specifies the following for the definition of related party that: "directly or indirectly control the Italian enterprise, or are controlled by it, or are controlled by the same company controlling the Italian enterprise". The Ministerial Decree of 14 May 2018 further explains in detail the "associated enterprises" and "control" terms as follows:

- "associated enterprises" means that they are enterprises either resident or non-resident of Italian territory where (i) one of them participates directly or indirectly in the management, control or capital of the other, or the same person participates directly or indirectly in the management, control or capital of both enterprises.
- "participation in the management, control or capital" means that the enterprise has more than 50% in the capital, voting rights or profits of another enterprise or it has a dominant influence over the management of another enterprise, based on equity or contractual constraints.

The Italian Tax Authorities gave a rather extensive interpretation to the concept of "control", deeming that the transfer pricing regime was applicable to all such cases in which a set of circumstances was indicative of a given company's influence, even if only potential, over the entrepreneurial decision of another. The Supreme Court aligned itself with the position of the tax authorities through its ruling N. 8130 of April 22, 2016, by upholding the Second Instance judges' ruling, pursuant to which the civil law notion of corporate control was not binding and therefore, transfer pricing rules should have been rightfully and duly applied. Hence, the concept of "control" must be extended to all hypotheses of economic influence that may be inferred from the single circumstances.

c) Nature of Transfer Pricing Documentation

There have been no laws issued to reflect and/or incorporate the criteria and recommendations provided in the OECD Guidelines of 1984 and 1995. The 1995 OECD Guidelines, on the other hand, have been informally translated for internal use by the Italian tax authorities and are considered the major reference.

This was until 2010 where formal regulations were issued referencing the 2010 OECD Guidelines and in subsequent guidelines the 2017 Guidelines were referenced. (see *Decision No. 137654 of the Commissioner of Italy Revenue Agency of 29 September 2010 on transfer pricing documentation requirements and Decision No. 0360494 of 23 November 2020 by the tax authorities*). The version of the OECD Guidelines in effect at the time transfer pricing regulations are applied should be used, and later editions of the OECD Guidelines should be ignored (*Regional Tax Court of Lombardy (judgment 3165 of 9 July 2015)*)

d) Tax Havens & Blacklists

Italy has abolished its own black-list (which was listed first in the Ministerial Decree of 4 May 1999 and amended from time to time) practice with the Stability Law that is enacted in 2016. Upon the question asked to Commission regarding the repeal of the black-list, Commissioner Pierre Moscovici answered that Italy is fully engaged in the process of developing a common EU approach towards third tax haven countries. Moreover, Italy's third country approach is consistent with the OECD's principles. Therefore, it can be said as well as EU's blacklist, OECD's point in tax havens is also appreciated in Italy.

e) Advance Pricing Agreement (APA)

Unilateral and bilateral APA are available. No fee is charged on APA application. APA's can be concluded with the Italia tax authorities by Italian resident companies or non-Italian resident companies which carry on or have the intention to carry on their business activity in Italy through a permanent establishment. The aims of APA can be: determine the methodology; attribution of profits to a permanent establishment in another state of an Italian company or determine the payment to foreign subjects residing in Italy or the receipt from a foreign subject residing in Italy, of dividends, interests, royalties and/or other income.

According to the Legislative Decree n.147/2015, the advance agreements provides:

- the definition of arm's-length price in intercompany transactions;
- the applications of norms on the allocation of profits or losses to the permanent establishment in another state, as well as on the payment to or receipt by non-residents of dividends, interests, royalties, and other income components; or
- prior definition of entry or exit values for residence transfers.

The legislative framework of Preventive Agreements has been upgraded by virtue of the so-called "Internationalization Decree" (Legislative Decree N. 147/7.10.2015) and its implementing regulation, i.e. Regulation N. 42295/21.3.2016 of the Italian Revenue Agency (IRA). The Internationalization Decree introduced the "Preventive Agreements for Enterprises with International Activities" (Preventive Agreements), substituting the previous "International Tax Ruling" (as per Art. 8 of Law Decree N. 269/2003). Presidential Decree N. 600/1973, where the aforementioned Internationalization Decree added Art. 31-ter, regulates the new instrument.

The Preventive Agreement shall be in principle valid for 5 years including the year of execution. However, it may also have retrospective effect in the following cases:

- it follows conclusion of agreement(s) with foreign tax authorities in the context of Mutual Agreement Procedure (MAP) under a Treaty; or
- it is based on the same factual and legal circumstances existing before its execution.

f) Audit Practice

Although Italian tax are taking the audits seriously, there is not an official approach yet. The number of the multinationals that are under scrutiny for transfer pricing practices keeps continuing a steady but increasing trend. Moreover, instructions of the Italian tax authorities occupy an important position on tax inspection activities and the introduction of transfer pricing documentation rules. During tax audits, the presence of transfer pricing documentation for multinational Italian companies is considered as an ordinary requirement in practice although filing is not mandatory as a rule.

3. Transfer Pricing Documentation

a) Level of Documentation

The Italian Revenue Agency has enacted a new AcT (Decision No. 0360494 of the Commissioner of Italy Revenue Agency of 23 November 2020) which renews and updates transfer pricing documentation requirements according to the OECD 2017 standards. These transfer pricing criteria remain optional, as they were previously: MNEs may choose to prepare a transfer pricing paperwork on their yearly corporate income tax returns in order to be protected by the Italian penalty protection framework.

The Transfer pricing documentation includes:

- the Master File;
- the National (Local) File;
- Country-by-Country reporting.

The Master File shall contain information about the group and shall be structured as follows:

- general description and structure of the Multinational Group;
- general strategies pursued by the Group and any changes of strategy compared to the prior financial year,
- related intercompany agreements,
- intercompany transactions and financing activities with information related to the group's financing structure to be included too,
- identification of entity(ies) in the group which provides central financing functions,
- functions, assets and risks;
- intangible assets (i.e. full list of the group's IP's),
- transfer pricing policy related to intra-group financial transactions,
- APA's and rulings concerning transfer pricing with the tax authorities of EU Member States as well as group consolidated financial statements.

It is possible to deliver more than one Master File if the MNE operates in different sectors each of them being governed by specific transfer pricing policies.

The National (Local) File shall contain information about the company and shall be divided as follows considering the latest changes:

- pre-existing requirements such as; (i) general description of the company, (ii) sectors in which the company operates, (iii) operational structure of the company, (iv) general strategies pursued by the company and any changes of strategy compared to the prior financial year, (v) intercompany transactions, (vi) cost contribution arrangements,
- a description of reporting lines regarding the employed human resources, including reorganization or transfers that affected the local entity in each local unit (that involves intangible assets),
- the explanation of multi-year analysis and its reasons, including comparability adjustments in order to provide greater reliability of results,
- statement of "main critical assumptions" that is used for applying certain TP method with assessments of the impacts which arise from the changes,
- detailed information on the financial data,
- a copy of the all types of APA's together with the cross-border rulings (which does not bind the resident company) that is relevant to the intra-group transactions included in the Local File.

The Country-by-Country Reporting shall contain information about:

- Amount of revenue;
- Profit and loss before income tax;
- Income tax actually paid;
- Income tax accrued;
- Stated capital;
- Accumulated earnings;
- Number of full-time employees and;
- Net book values of tangible assets.

The first tax year of application of the regime about Country-by-Country Reporting in Italy is 2016.

The obligations about Country-by-Country Reporting refer exclusively to Italian parent companies of MNE Groups that:

- have annual revenue equal to or exceeding € 750 million per year starting from 1 January 2015;
- are required to file group consolidated financial statements;
- are not controlled by any other entities.

Holding companies or permanent establishments of holding companies are required to present the Master File as well as the National File. If the threshold revenue (€ 750 million) is exceeded the Italian parent companies have an unconditional obligation to file Country-by-Country Reporting with the Italian Revenue Agency.

Sub-holding companies and permanent establishments of sub-Holding companies are required to present the Master File as well as the National File. A sub-holding company can present together with the National File, the Master File prepared by its non-resident holding company.

Controlled companies and permanent establishments of controlled company are only required to present the National File. The Italian subsidiaries have to comply with Country-by-Country Reporting obligation only in case the Italian Revenue Agency is unable to obtain Country-by-Country Reporting or equivalent report regarding the respective multinational group from another source, e.g. in lack of equivalent obligation of the parent company in its residence jurisdiction.

b) Industry Analysis

By identifying value drivers for the relevant industry, a first indication of the level of profitability common in the industry is being given.

c) Company Analysis

A description of the management structure of the local entity, a local organisation chart, and a description of the individuals to whom local management reports and the country(ies) in which such individuals maintain their principal offices.

A detailed description of the business and business strategy pursued by the local entity including an indication whether the local entity has been involved in or affected by business restructurings or intangibles transfers in the present or immediately past year and an explanation of those aspects of such transactions affecting the local entity.

d) Functional Analysis

In conducting a functional analysis, an assessment is made of the significant activities and responsibilities that are performed by the related parties relevant to the Intercompany Transactions under review, the tangible and intangible assets that are employed and the risks that are borne in undertaking the business activities.

Such an assessment is consistent with the recommendations that have been made in the OECD Guidelines at paragraph 1.51.

e) Choice of Transfer Pricing Method

Since the Transfer Pricing Methods in the OECD Transfer Pricing Guidelines 2017 is fully adopted, there is no other hierarchy set. That includes transaction-based methods and profit-based methods although the Circular No. 32/1980 considers the hierarchy of methods.

Transaction-based methods are preferred to profit-based methods, and CUP method is preferred to other methods. In case of the usage of any alternative methods, sufficient explanations must be given if it is also possible to apply CUP or any other transaction-based methods.

f) Economic Analysis – Benchmark Study

In Italy, there is no explicit preference or recommendation for internal comparables. When using the CUP technique, however, the Circular (chapter III, section 1) states that internal comparables should be used wherever available. See for further reference also the Supreme Court judgements 22010 of September 25, 2013 and 24005 of October 23, 2013, as well as the Regional Tax Court of Lombardy in its judgment 335 of February 6, 2020.

When internal comparables are available, the RPM technique should be favoured over the TNMM approach, according to the Regional Tax Courts of Lombardy (decision 3554 of September 23, 2019) and Lazio (judgment 5261 of September 24, 2019).

In Italy, there is no explicit preference or guideline for external comparables. External comparables are normally identified through the use of one or more databases, and the OECD Guidelines are often followed. The OECD Guidelines should be followed to locate and pick external comparables, according to the Milan Provincial Tax Court (judgment 7198 of 14 September 2015). See also judgements of the Regional Tax Court of Lombardy (judgment 3165 of 9 July 2015) and the Provincial Tax Court of Milan (judgment 4749 of 12 November 2019) where guidelines regarding ATECO codes were established. It is not permissible to use external comparables with a different ATECO code than the tested party. Using solely the ATECO codes of other firms to locate and select relevant external comparables is ineffective. The entire turnover and the company's purpose as determined by the bylaws (oggetto sociale) should also be considered. Furthermore, tax authorities are not permitted to dismiss enterprises that made a loss during the tax year in question.

Where it comes to the CUP approach, the Circular (chapter III, section 1a) states that "when the foreign market is significant, but the Italian market exhibits identical traits (a hypothesis that, while plausible, happens very seldom), the reference to the Italian market is seen as preferred." In Italy, however, there is no explicit guideline on international comparables or hidden comparables.

g) Inter-company (IC) Legal Agreement

Although an Inter-company legal agreement formalizes the business and financial relationship between group entities, the legal agreements have a lower ranking since the OECD 2017 Guidelines made the "conduct of parties" the prevailing concept.

h) Financial Statements

This section is not applicable.

i) Production Process for TP Relevant Returns, Documents, Forms and Financials

In the chart below, the existence of the filing requirements with the details of which format is used, the latest filing date, notification requirement and its deadline, thresholds to be applied in case it exists, and the required languages are demonstrated. This information can be seen respectively for CIT, master file, local file, CbCR, local forms, annual accounts, and segmented P&L documentation.

	Prepare or File?	Format	Deadline	Notification Deadline*	Threshold* (Yes/No)	Local Language (Yes/No)*(If "No", it can be filed in English)
Corporate Income Tax	File	Local GAAP	November, 30 th .	No	No	Yes
Master File	Prepare (digital signature)	OECD Guidelines	November, 30 th .	No	Yes	Yes
Local File	Prepare (digital signature)	OECD Guidelines	November, 30 th .	No	Yes	Yes
CbCR	File	OECD Guidelines	November, 30 th .	Yes	Yes	Yes
Local Form	File	RS 106	September, 30 th .	No	No	Yes
Annual Accounts	N/A	N/A	N/A	N/A	N/A	N/A
Segmented P&L	Yes	Electronic	November, 30 th .	No	No	Yes

* Italy has signed the MCAA agreement for the filing of CbCR.

* SME's are defined as companies with turnover or revenues of maximum EUR 50 million. They have the right not to update the information relevant to the transfer pricing method for the two years following the year concerned if both:

- the comparability analysis is based on publicly available sources; and
- the key features of goods and services, the analysis of the functions, assets and risks, the contractual terms, the economic conditions and the strategies of the company do not undergo significant changes.

The availability of transfer pricing documentation must be disclosed to the tax authorities. Intercompany transaction volumes must also be disclosed. In addition, companies should tick the box in the income tax return form that indicates it has been prepared with proper documentations, to be protected against penalty regime.

Generally, deadline for the submission of the tax return is the 30 September of the year following the tax years. Transfer pricing documentation must be prepared simultaneously with the tax return.

Deadline for the submission of Country-by-Country Reporting is due 12 months from the last day of the relevant tax year, this, in essence, implies that the first Country-by-Country Reporting shall be filed in Italy by the end of 2017.

Upon request of the tax administrative, taxpayers must supply the transfer pricing documentation within 10 days and any supplemental information within seven days or other terms agree with. According to the Italian law tax audits must be finalized in a maximum of 30 working days, which can be extended by additional 30 days.

According to the stability law of 2016, a tax assessment for income tax can be issued up to 31 December of the fifth year following the year when the relevant tax return was submitted to the tax authorities. In case of failure to file annual tax return, the statute of limitations is extended to 31 December of the seventh year following the year in which the tax return should have been filed. For the fiscal years prior to 2016 still are subject to the previous rules: the statute of limitations is 4 years following the tax year and one year extension is granted in case of failure to file annually tax return. This period is double if taxpayers incur in criminal tax purposes, under certain conditions.

j) Mandatory Language

Both the Master File and the National File must be written in Italian. However, the Master File of a sub-holding can be presented in English when presenting the Master File of a non-resident company. Attachments can also be presented in English. Attachments in any language other than Italian or English have to be translated into Italian. No specific formats are prescribed for Country-by-Country Reporting, but it should be drawn up in at least one official EU language (in Italy both Italian and English).

k) Notification Requirement

According to the Italian legislation¹, Italian MNE's who are the Ultimate Parent Entities that have annual turnover equal to, or more than €750 million in the preceding FY must submit an annual CbCR. The provisions prescribe an automatic exchange of CbC reports mandatory between the EU member states. The mandatory report should include amongst others; revenue amounts, profit/loss before taxes, taxes paid and accrued, accumulated earnings, the number of the employees, tangible assets, and other indicators of economic activities. The deadline for filing is 12 months and for notifying is 11 months after the last day of the reporting period.

l) Record Keeping

Records must be kept for at least 10 years.

m) Penalties and Interest Charges

No transfer pricing specific penalties apply. General penalty provisions can result in penalties from minimum 90% to maximum 180% of the additional tax due as a result of a transfer pricing adjustment. No interest is charged on penalties, but on the additional taxes generated by transfer pricing adjustments.

Legislative Decree No. 74 of 10 March 2000 permits tax inspectors to refer assessments to the public prosecutors to explore possible criminal tax law implications.

Article 26 of law-decree No. 78 of May 31, 2010 provides that, in the case of a transfer pricing assessment, no penalties will be levied if the taxpayer both complies with specific documentation requirements and a specific communication is filed with the Italian tax authorities.

¹ Provisions n. 275956 and n. 288555.

In accordance with the Budget Law for 2016, non-compliance with the Country-by-Country reporting obligations, the administrative sanctions amounting to € 10.000 – € 50.000. Non-compliance may refer for example to lack of filing of Country-by-Country Reporting or provision of incomplete or inaccurate information.

The disapplication of penalties is linked to the revenue office's assessment on the suitability of the TP documentation provided.

Suitability must be ascertained from a formal standpoint based on:

- The consistency of the documentation compiled by the taxpayer;
- The nature and structure of such documents set forth in explanatory regulation issued by the Italian Revenue Agency issued on September 29 2010 (Measure 137654/2010); and
- A substantial perspective, examining the suitability of the documents compiled by the taxpayer to provide the revenue office with whatever data and findings that will be necessary to carry out a comprehensive and thorough analysis of the transfer prices that were actually applied.