Tax Connect Flash

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Italy: Tax authorities released the first bulletin on international tax rulings

The bulletin, released on April 21, 2010, summarizes, for the first time, for statistical purposes and anonymously, the outcome of the requests for the international ruling procedure made under Italian tax law.

The data shows that, in the period 2005-2009:

- 52 applications (out of which 7 not admissible) had been submitted in the concerned period with an average of 10 per year;
- 19 binding agreements were signed with the Italian tax authorities, with an average of 4 per year;
- The average time needed to reach the agreement is approximately 20 months;
- More than 50% of the Advance Pricing Agreements (hereinafter "APAs") concluded with the Italian tax authorities used the TNMM as the preferred transfer pricing method.

Background

Article 8 of the Law decree No. 269 of September 30, 2003 – implemented with the Regulation of the Director of the Revenue Agency of July 23, 2004 – introduced, under Italian tax, the "international ruling procedure" with effect starting from February 2005 (date of the favorable opinion of the European Commission).

The international ruling procedure is addressed to companies with international activity that intends to agree in advance with the Italian tax authorities:

a) the transfer pricing methodology applicable to transactions carried on with related parties in the form of unilateral APAs;

b) the application of tax treaties distributive rules to specific cases;

c) the attribution of profits to permanent establishments (hereinafter "PE" or "PEs").

Access to the international ruling procedure is made, on a voluntary basis and free of any charge, by mean of an application sent to the International Ruling Office – International Division – Central Directorate for Tax Assessment of the Revenue Agency, which is organized in two branches based in Rome and Milan.

Within 30 days from the receipt of the application, the International Ruling Office schedules a first meeting with the taxpayer in order to define the terms and developments of the procedure. The procedure follows with several meetings during which further documentation may be required and visits to the premises where the business is actually carried on may be organized in order, for the Italian tax authorities, to obtain direct knowledge of the circumstances represented in the application.

The procedure should be completed within 180 days from the date in which the application is filed. Nevertheless, as this term is merely formal, according to the circumstances, the parties may agree to extend the procedure.

The procedure ends up, possibly but not mandatorily, with a 3 years binding agreement between the taxpayer and the Italian tax authorities which sets out the criteria and methods for calculating the normal value of the transactions to which the application refers, or, in other cases, the criteria for application of tax treaties.

During the 3 years period the Revenue Agency, and more specifically the International Ruling Office, verifies that the terms of the agreement are complied with and also ascertains whether any changes have occurred to the de facto or de jure conditions which constitute the assumptions on which the clauses of the agreement are based. This activity is carried out also by means of one or more visits to the premises where the enterprise carries on business.

At the end of the 3 year period of validity, and at least 90 days before it expires, the taxpayer may submit an application for renewal. Starting from 2008, 4 agreements have been renewed.

Statistics on the application of the international ruling procedure

We summarize here-below some of the data provided by the Italian tax authorities in the first bulletin on international tax rulings.

- **Table 1**: Applications for the international ruling procedure in 2004-2009
  The data provided in Table 1 shows that 52 applications have been submitted in the period 2005-2009 with an average of 10 per year. However, out of the 45 out applications not rejected only 19 ended up in a binding agreement between the taxpayer and the Italian tax authorities with an average of 4 per year.

Applications submitted	52
International ruling granted	19
Procedures in process as at December 31, 2009	17
Applications rejected due to the lack of subjective or objective elements	7
Applications withdrawn	9

- **Table 2**: International ruling procedure completion time (months per procedure)

  Table 2 shows the procedures concluded in relation to the number of months necessary to be signed.

  The duration has been calculated as the difference between the date of signature of the agreement and the date of submission of the application. Calculation of this difference excludes any suspension periods due to the lack of essential elements to reach the agreement. Instead, the duration of the procedure includes periods of inactivity or delay in providing documentation or information from the taxpayer.

  The average time, approximately 20 months, is calculated as a simple average of the total number of months necessary to sign the agreements.

Months	No. of agreements signed
5	1
6	1
8	1
10	1
11	1
14	1
15	2
17	2
20	1
21	2
22	1
25	1
27	1
34	1
35	1
48 months or more	1
Completion time: average months	**20**

- **Table 3**: Methods used for determining APAs

Description of methods	No. Cases Partial	No. Cases Total
Comparable Uncontrolled Method (CUP)		1
Internal comparables	1	
External comparables		
Cost Plus Method (CPM)		3
Internal comparables	2	

External comparables	1	
Resale Price Method (RPM)		
Internal comparables		
External comparables		
Transactional Net Margin Method (TNMM)		10
PLI (profit level indicator): mark-up on total cost	7	
PLI (profit level indicator): return on sales	3	
Profit Split		5
Contribution analysis		
Residual analysis	5	
Total		**19**

- **Table 4**: Classes of taxpayers by turnover

  Table 4 shows the data relating to taxpayers, divided into classes according to turnover, who signed an agreement or whose procedure was still pending as of 31 December 2009. The data shows that the majority of taxpayers submitting applications (approximately 52%) have a turnover of 300 million Euro or less, and 37% of these fall into the class of taxpayers with turnover of more than 300 million Euro.

Taxpayers' turnover	Number of taxpayers*	%	Average % of the cross-border transactions (between related parties) covered by ruling on the total of cross-border transactions
Turnover < 100M Euro	13	48.15%	82.78%
Turnover from 100 to 300M Euro	4	14.81%	79.21%
Turnover > 300M Euro	10	37.04%	47.75%
Total	**27**	**100%**	

* The total number of taxpayers indicated does not coincide with the data provided in Table 1 because a single taxpayer submitting more than one application has been counted only once.

Tables 5 and 6 show the ruling procedures which were concluded with an agreement distinguished on the basis of the relationships between the associated parties and the type of transactions covered by ruling agreements.

- **Table 5** shows roughly the same number of companies which are controlled by non-resident subjects and companies which carry out transactions with subsidiary companies abroad.

Relationships between associated parties	No. of transaction in the agreements signed*
Non-resident parent company – Italian subsidiary**	9
Italian parent company – non-resident subsidiary	8
Italian related company – non-resident related company	6
Italian PE – non resident head office	2
Non-resident PE – Italian head office	0

* 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 as the scope of an agreement may also include more than one kind of relationships between related parties.
** The concept of control includes both direct and indirect control.

- **Table 6** shows a predominance of agreements concerning the sale of tangible goods from Italy (50% of total transactions).

Relationships between associated parties	No. of transaction in the agreements signed*
Sale of tangible property into Italy	11
Purchase of foreign goods	4
Performance of services by Italian entity	3
Performance of services by non-Italian entity	0
Cost sharing agreements	1
Transactions involving intangible property	1
Attribution of profits to a PE	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 as per Table 1, since an agreement may also include more than one kind of transactions between related parties.

Our considerations

The data provided by the Italian tax authorities shows that it takes quite a long time to complete the international ruling procedure. Notwithstanding the length of the procedure and the fact that the Italian tax authorities apply a one-side approach, the international ruling procedure may be a an instrument to reduce tax risks on cross-border transactions.

As a matter of fact, as the recently issued circular letter No. 20/E of April 16, 2009 proves (see the Italian tax alert of May 10, 2010), the Italian tax authorities are paying more and more attention to transnational transactions.

How we can help

CMS has a network of international tax specialists that can help you in submitting international tax rulings before the Italian tax authorities. We also have a network of transfer pricing specialists that can support you in discussing APAs with the Italian tax authorities.

For further information on this tax analysis and thought, please contact:

Fabio Aramini
Partner– CMS Adonnino Ascoli & Cavasola Scamoni
E fabio.aramini@cms-aacs.com

Giovanni B. Calì
Partner – CMS Adonnino Ascoli & Cavasola Scamoni
E giovanni.cali@cms-aacs.com