

Clarification on TP documentation in Italy starts moving forward

Federico Vincenti and Alessandro Valente of Valente Associati GEB Partners/Crowe Valente discuss the public consultation in relation to the transfer pricing documentation requirements for the correct application of the arm's-length principle in Italy.



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Circular published on September 20 2021 to clarify TP documentation in Italy

On September 20 2021, the Italian Revenue Agency (IRA) published the draft circular letter (the Circular) aimed at providing a vast range of clarifications on the transfer pricing (TP) documentation's legal framework.

The Circular has been drafted to provide further operational instructions on the changes introduced by the Administrative Provision No. 360494 of November 23 2020 (containing the new rules on TP documentation).

The Circular was released for public consultation for comments and proposals. The consultation closed on October 12 2021.

One of the most significant changes concerns the obligation of digital signature with the time stamp of the master file and local file. Indeed, before the date of submission of the tax return for the relevant tax year (i.e. November 30 2021), the two documents must be digitally signed and temporally marked by the legal representative of the taxpayer or his delegate.

The draft circular letter emphasises, once again, the function and objectives of the TP documentation.

In particular, according to the Circular, the predisposition of suitable TP documentation allows taxpayers to benefit from the non-application of sanctions in case of TP adjustments by the Italian Tax Administration.

This TP regime is based on the recognition of commitment and good faith of taxpayers, who are required to prepare appropriate TP documentation in order to ease the assessment of compliance with the arm's-length principle by the tax authorities.

Companies must prepare both the master file and the local file according to the structure provided for by Provision No. 360494 of November 23 2020. If all the prescribed conditions are met, the TP documentation can qualify as suitable and taxpayers are entitled to benefit from the penalty protection regime.

The administrative provision specifies that the master file and the local file must be prepared in Italian. However, the master file may be prepared in English, given that in some countries this document must be prepared and submitted according to the OECD standards.

The possibility for small and medium-sized enterprises not to update (for a maximum of three years) certain data and elements of intra-group transactions included in the local file, is confirmed. This simplification aims at reducing administrative burdens and compliance costs for small taxpayers (with revenues not exceeding €50 million).

Such simplification will be granted only if the comparability analysis is based on information obtained from publicly available sources and provided that the elements referred to the five comparability factors are not significantly modified in the tax periods concerned.

The administrative provision provides for the possibility of submitting more than one master file if the group carries out different activities governed by specific TP policies (so-called divisions).

In addition, the Circular describes the content of the master file and the local file, providing clarifications on further novelties introduced by the provision, such as:

- The possibility for the taxpayer to submit the appropriate documentation concerning only part of the transactions carried out;
- The documentation required to apply the so-called 'simplified approach', as regards low value-added services; and
- Application of the time stamp and communication in the tax return.

The master file should include all the essential information in order to describe the organisational structure of the group (supplementary worksheets and diagrams to illustrate the legal and ownership structure of the MNE group and the local entities' location), the general representation of the activities carried out by the group, transaction flows, a list and a brief description of the main contracts or agreements governing the provision of intra-group services, APA and MAP.

The Circular confirms that the rules set out in the administrative provision apply to permanent establishments of non-resident companies and resident companies with permanent establishments abroad. Moreover, it specifies that as regards transactions between the permanent establishment and the entity to which it belongs, the so-called 'authorised OECD approach' or 'AOA' adopted by the OECD should be followed.

According to the Circular, the TP documentation should be considered suitable when it allows the tax administration to fully understand the TP policies adopted by multinational groups (even if the company at issue has not selected the correct method or the tax administration has questioned the selected comparables).

Partial omissions or inaccuracies (e.g. failure to document transactions that are marginal compared to the overall intra-group transactions) may not affect the application of the penalty protection regime if they are not likely to compromise the supervisory bodies' analysis and the correctness of the results of that analysis.

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