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The Italian Advance Pricing Agreements

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The International Ruling Office (the Office) of the Agenzia delle Entrate (the Italian Revenue Agency) has finally released the second issue of the Bulletin, almost three years after the release of the first issue. Establishing Advance Pricing Agreements (APAs) with Italian companies engaged in intercompany cross-border operations forms 89 per cent of the Office's activities. The Bulletin can therefore be considered as the official publication of Italian APAs.

APA applications and signed agreements have increased significantly in recent years as a consequence of an increasingly aggressive approach by the Italian tax authorities towards transfer pricing audits. An APA, which is valid for three years, is being considered more and more as a valuable solution for multinational groups with Italian operations to guarantee certainty on their transfer pricing policy.

Ruling Applications

Since the Office opened in 2004, 135 ruling applications (not all relate to transfer pricing issues) have been filed and 56 ruling agreements have been concluded.

According to the Bulletin, while only 52 applications were filed in the whole period 2004 to 2009, 83 applications have been filed in the last three years (2010-2012) alone, 38 of which were filed in 2012. The volume of agreements has also increased substantially in recent years: 30 of the 56 ruling agreements were concluded in just the last two years, 11 in 2011 and 19 in 2012.

As at 31 December 2012, 54 ruling procedures were in progress and another 25 ruling applications had been dismissed, owing to the lack of some of the necessary requirements, information or documents, or were withdrawn by the taxpayer.

Advance Pricing Agreements

The international ruling is basically a unilateral tool in that it results in an agreement between the Italian tax authorities and the taxpayer, but does not involve the tax authorities of the other jurisdiction(s) where the taxpayer operates. Since 2010, however, the Office has been entering into bilateral or multilateral APAs. According to the Bulletin, 19 bilateral APAs were in progress as at 31 December 2012, including four with the United States, three with Germany, and one each with

France and the United Kingdom.

The APA procedure is activated by the taxpayer on a voluntary basis and is not subject to any activation fee. The taxpayer can also apply for a pre-filing meeting, even on a no-name basis, to consult the Office on a preliminary, informal and generic basis. The Bulletin indicates that, over the last four years (2009-2012), 110 pre-filing meetings were held, 91 of which with full disclosure of the taxpayer's identity and 19 on a no-name basis. Transfer pricing issues were discussed in 75 per cent of the pre-filing meetings; other topics included dividends, interest and royalty payments (12 per cent), attribution of profits to a permanent establishment (5 per cent), cost sharing agreements (4 per cent) and business restructurings (4 per cent).

A standard APA procedure involves one or more meetings with the Office, and may also include the tax authorities visiting the taxpayer's premises in order to acquire direct knowledge of the facts described in the ruling application. As a general rule, the procedure should be completed within 180 days of the filing of the application; however, this term is often disregarded. The Bulletin indicates that the average length of the APA procedure is actually 16 months, in line with European standards, although 16 per cent of the signed APAs took more that 24 months to complete. Significantly, the average length of the procedure is decreasing: it was 20 months when the first issue of the Bulletin was released in 2010.

Transfer Pricing Issues

The Bulletin indicates that the Office and the taxpayer agreed the transfer pricing method to be applied to determine intercompany prices in 43 APAs. In nine cases, a traditional transaction method was selected (four cases comparable uncontrolled price, three cases cost plus, two cases resale minus). In the remaining 34 cases a transactional profit method was agreed (24 cases transactional net margin method (TNMM), 10 cases profit split). When the TNMM was selected, in 17 cases the mark up on total costs was identified as the profit level indicator (PLI), while in the remaining seven cases the identified PLI was the return on sales. As regards the profit split method, the residual approach was followed in all 10 cases.

Sectors

The APAs covered transfer pricing in manufacturing (42 per cent of the cases), distribution (37 per cent) and services transactions (21 per cent).

As to the identity of the taxpayers applying for an APA, 68 per cent of applicants overall qualify as "large taxpayers", i.e., taxpayers with an annual turnover higher than €100 million. Applicant taxpayers are split between manufacturing (52 per cent) and trading and services (48 percent), and span many industry sectors, including tobacco, transportation, banking and insurance, telecommunications and IT.

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