



### IN THIS EDITION

1. New provisions for transfer pricing documentation

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### **New provisions for transfer pricing documentation**

For all clients

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The provision of the Director of the Revenue Agency (protocol no. 2020/360494) published on 23 November 2020 updates the Italian provisions on transfer pricing documentation, aligning the same with the OECD guidelines (latest version of 2017).

The new indications replace those of the 2010 measure (protocol no. 2010/137654) starting from the tax period current on 23 November 2020.

Consequently, taxpayers will be required to apply the new guidelines for the documentation relating to the year 2020 to be prepared during 2021 (by 30 November 2021 for those whose tax period follows the calendar year).

Below is a summary of the most important innovations introduced by the recently published measure:

- a) All entities resident or established in Italy belonging to multinational groups that undertake intercompany transactions with foreign group entities are required to prepare transfer pricing documentation. Also included are permanent establishments in Italy of non-resident companies and permanent establishments abroad of companies resident in

the Italian territory. The distinction by categories of enterprises (holding, sub-holding, subsidiary) is therefore eliminated.

- b) The appropriate documentation in order to benefit from the so-called *penalty protection* (i.e. the non-application of penalties for untrue tax return in case of adjustment by the tax authority of the arm's length value of the transfer prices applied within the group) consists of both the following documents: Masterfile and Local File.
- c) The structure and content of the Masterfile and the Local File are modified and aligned with the provisions of Chapter 5 of the OECD Guidelines.

The Masterfile provides an overview of the group's activities and the factors that contribute to the creation of value within the group, allowing tax authorities to frame the transfer pricing policies adopted by the group in their (economic, legal, financial and fiscal) reference context, and thus to carry out a global risk assessment.

The Local File, on the other hand, refers to intercompany transactions undertaken by the resident entity, allowing the verification of compliance with the arm's length principle.

In this regard, it should be noted that the main changes made to the documents concern the following aspects:

#### Masterfile

In the Masterfile - which may be drafted in English - more details are required on the activities carried out by the group (important drivers of business profit, description of the supply chain for the group's five largest products and/or service offerings by turnover plus any other products and/or services amounting to more than 5% of group turnover) and on certain categories of transactions, such as intercompany services, intangible assets, financial transactions. It is for example required to describe the capabilities of the principal locations providing important services; the activities carried out for the development, ownership and exploitation of intangible assets and related research and development agreements; the financing methods and central treasury functions. It is required to attach the consolidated financial statements of the group and to describe all Advance Pricing Agreements (APA) and prior cross-border ruling agreements signed with, or issued by, the tax authorities of the countries in which the group operates.

#### Local File

A more detailed breakdown is required of the comparability analysis, of any comparability adjustments applied to the tested party and/or comparable parties, as well as of the critical assumptions adopted while applying the chosen transfer pricing method. In addition, it is necessary to attach: (i) the annual local entity financial accounts for the

fiscal year concerned, including the audit report; (ii) reconciliations schedules between the financial data used for the application of the transfer pricing method and the financial statements data; and (iii) in addition to a copy of all intragroup agreements related to the transactions described, copies of existing unilateral and bilateral/multilateral advance pricing agreements and prior cross-border rulings to which the domestic enterprise is not a party, but which are nevertheless related to the intercompany transactions subject to documentation.

- d) Specific documentation should be prepared in case of use of the simplified approach on low value-adding services (as authorised by article 7 of the Ministerial Decree of 14 May 2018 which provides guidelines for the application of transfer pricing provisions). Specifically, the following is required:
- detailed description of the services, the reasons for the provision and the underlying contracts, the beneficiaries and the related benefits obtained or expected, as well as the allocation criteria applied;
  - illustration and documentation of the cost base and calculations supporting the application of the allocation criteria.
- e) Small or medium-sized enterprises (i.e. companies with a turnover or revenues not exceeding 50 million euros in the reference tax period) are entitled not to update the data included in the paragraphs relating to intercompany transactions in the Local File, for the two tax periods following the one to which the documentation refers, provided that the comparability analysis is based on information obtained from publicly available sources and that no significant changes in terms of analysis of economically relevant characteristics and functional analysis have occurred in such tax periods.

However, the new measure limits the definition of small or medium-sized enterprises as it does not include entities that directly or indirectly control or are controlled by an entity that does not qualify as a small or medium-sized enterprise.

- f) It is possible to submit documents for only a part of the intercompany transactions carried out. In this case, the possible disapplication of administrative penalties shall be applied with exclusive reference to the transactions described and considered suitable for this purpose.
- g) The documentation shall have certified date. The Masterfile and the Local File must in fact be signed by the taxpayer's legal representative, or his delegate, by means of an electronic signature with time stamp to be affixed within the filing date of the tax return.
- h) Modification or integration of the documentation is allowed in the case of filing of a supplementary tax return for errors or omissions concerning intercompany transfer prices

(i.e. resulting from non-compliance with the arm's length principle) and the related communication shall be provided in the same supplementary tax return.

- i) The deadline for the delivery of the documentation, in the event of a specific request by the tax authority, is extended from 10 days to 20 days.
- j) During tax audits, control officers giving a negative judgement on the appropriateness of the delivered documentation shall provide specific reason and motivation for this. In any case, the power of the competent office to critically assess this judgement for the purpose of imposing penalties remains unaffected.

Finally, it should be noted that large multinational groups (with a consolidated turnover, in the tax period prior to the reporting period, of at least 750 million euros), are also required to prepare the "Country-by-Country Reporting".

Our consultants are at your disposal to advise you on transfer pricing and related matters and to assist you in the preparation of the relevant documentation.



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