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Global Tax Alert

News from Transfer Pricing

Italy issues Ministerial Decree implementing Country-by- Country Reporting

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Executive summary

On 8 March 2017, the Italian Ministry of Economy and Finance released the Ministerial Decree (the Decree) with implementation details of the Country-by-Country Reporting (CbCR) process for Italian entities belonging to Multinational Enterprises (MNE) Groups, introduced by the 2016 Budget Law¹ (the Law).²

As background, the Law introduced a CbCR obligation for MNE Groups to submit an annual report indicating the amounts of revenue, profit before taxes, taxes paid and accrued, and other indicators of effective economic activities starting from the Fiscal Year (FY) commencing on 1 January 2016, or afterwards (reporting period).

The requirements of the Italian CbCR rule are generally in line with the Organisation for Economic Co-operation and Development (OECD) guidance on CbCR³ and the 2016 European Union directive (EU Directive) on CbCR.⁴

Detailed discussion

Definition of MNE Group members

For purposes of the CbCR, the following entities are considered to be MNE Group members:

- (a) Any entity included in the consolidated financial reporting, or that would have been included if the shares of such entity were traded on a public securities exchange.
- (b) Any entity excluded from the consolidated financial reporting due to their size or materiality.
- (c) Any permanent establishment (PE) of an entity compliant with subparagraphs (a) and (b) above, if the PE prepares separate reporting for accounting, tax and management purposes.

Primary reporting obligation

The Ministerial Decree introduces CbCR filing obligations for Italian parent companies of MNE Groups that: (i) are required to file group consolidated financial statements; (ii) have realized a consolidated annual turnover in the FY preceding the reporting period of at least €750 million; and (iii) are not controlled by any other entities.

Secondary reporting obligation

- ▶ **Local filing:** Italian subsidiaries of an MNE Group are required to file a CbC report, if the foreign parent entity is resident for tax purposes in a country that: (i) has not implemented the CbCR; or (ii) does not have a Qualifying Competent Authority Agreement in place with Italy for the automatic exchange of information contained in the CbC report; or (iii) has incurred a systemic failure to exchange the information contained in the CbC report received by the parent company resident in its jurisdiction.
- ▶ **Surrogate Parent Entity (SPE):**⁵ Similar to the provisions of the EU Directive, in case one of the conditions for local filing occurs, the MNE Group may designate another entity of the MNE Group to file the CbC report in its own jurisdiction on behalf of the parent company. Filing by the SPE would relieve the obligation for local filing as long as the following conditions are met:
 - The jurisdiction of the SPE has implemented CbCR
 - The jurisdiction of the SPE has a Qualifying Competent Authority Agreement in place with Italy for filing the CbC report in the Reporting Fiscal Year
 - The jurisdiction of the SPE has not notified the Italian Tax Administration of a systemic failure
 - The Italian Tax Administration has not notified the local subsidiary of a systemic failure of the SPE's jurisdiction

- The SPE has notified its status to its own tax jurisdiction by the last day of the reporting period
- The Italian entity properly notified the Italian tax administration

- ▶ **EU designated entity:** MNE Groups with subsidiaries in more than one EU Member State may designate an EU designated entity to file the CbC report in one Member State that would then have the obligation to communicate the information contained in the CbC report with other relevant EU Member States. Filing by the EU designated entity would relieve the obligation for local filing in Italy. If the EU designated entity is resident for tax purposes in Italy, it must notify the Italian Competent Authorities that its CbC report filing is intended to satisfy the filing requirement of all members of the MNE Group that are resident for tax purposes in the EU. If such entity cannot obtain all the necessary information to file the CbC report by the Ultimate Parent Entity (UPE), it must notify the Italian Tax Administration that it has not received all the required information.
- ▶ **Voluntary filing:** The obligation for local filing in Italy is relieved if the UPE of the MNE Group, resident for tax purposes in a jurisdiction that has not yet implemented the CbCR obligation, files the CbCR on a voluntary basis with the Competent Authorities of its tax jurisdiction. Such relief is available only for the FY in progress on 31 December 2016, provided that the following conditions are met:
 - The CbC report is submitted by the UPE to its Competent Authorities within 12 months from the last day of the reporting period
 - The Constituent Entity's tax jurisdiction introduces the obligation to file the CbC report within the deadline set for the submission of the first reporting year
 - By the due date of the first reporting year, a Qualifying Competent Authority Agreement is in place between Italy and the jurisdiction in which the UPE is resident for tax purposes
 - The jurisdiction of tax residence of the UPE has not notified to the Italian Competent Authorities a systemic failure
 - The Italian resident entity notifies the Italian Competent Authorities of the identity and tax residence of the reporting entity

Timing of filing and exchange of CbCR

By the due date of the tax return related to the first reporting period, Italian resident entities of MNE Groups are required to notify the Italian tax administration of:

- a. Their own status as UPE, SPE or EU designated entity.

Or

- b. The identity and tax residency of the UPE, SPE or EU designated entity.

The communication will occur taking into account the procedures provided for filing the income tax return.

The content of the CbC report is aligned with the OECD guidance. Further instructions on the submission mechanism and language will be provided in Operational Instructions to be issued by the Italian Revenue Agency.

In compliance with the EU Directive, the CbC report should be filed with the Italian Competent Authorities within 12 months from the end of the reporting period. The Italian Tax Authorities will then exchange the CbCR with the EU Member States and any other jurisdiction with which Italy has a Qualifying Competent Authority Agreement within 15 months (18 months for the first reporting period) from the last day of the fiscal year to which the CbCR relates.

Penalties

No reference to penalties is made in the Ministerial Decree. However, as provided by the Law, in the case of omission or incomplete submission of the CbC report, penalties apply from €10,000 to €50,000.

Use of the information

The Italian Revenue Agency will leverage information contained in the CbC report to assess transfer pricing risks and other risks related to base erosion and profit shifting.

The Ministerial Decree clarifies that transfer pricing adjustments cannot be made purely based on CbCR information. However, such information may give rise to further investigations on intercompany agreements or during tax audits, leading to potential adjustments to the taxable income.

Liaison with Italian transfer pricing documentation regime

The Ministerial Decree does not clarify the relationship between the existing Italian transfer pricing documentation regime for penalty protection purposes and the documentation requirements provided by Action 13 of the BEPS project. In fact, while the former is prepared on a voluntary basis and entails a strategic management decision, the latter seems to require the mandatory existence of the three components (Master file, Local file and CbC report).

Endnotes

1. Law n. 208 of 28 December 2015.
2. See EY Global Tax Alert, [Italian Parliament issues budget law for 2016 including Country-by-Country Reporting and other important tax measures](#), dated 31 December 2015.
3. OECD Base Erosion and Profit Shifting (BEPS) Action 13.
4. Directive 2016/881/EU of 25 May 2016 amending Directive 2011/16/EU.
5. The Surrogate Parent Entity is defined as one Constituent Entity of the MNE Group that has been appointed by such MNE Group, as a sole substitute for the Ultimate Parent Entity, to file the CbC report in that Constituent Entity's jurisdiction of tax residence, on behalf of such MNE Group.

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