New Guidelines from Tax Authorities on Management of Tax Disputes under Mutual Agreement Procedures

The Italian tax authorities issued guidance in June 2012 on the management of tax disputes under mutual agreement procedures. The authors consider this guidance along with its interaction with the EU Arbitration Convention and the OECD Model Convention.

1. Introduction

According to data collected by the OECD in collaboration with member and non-member countries, in the five-year period from 2006 through 2010 the number of mutual agreement procedures (MAPs) opened to settle international disputes on the subject of double taxation increased by more than 40%. This international trend is also reflected in statistics published in Italy: in the two-year period from 2009 through 2010, there were 53 procedures initiated involving the Italian tax authorities (31 in 2009 and 22 in 2010), with an increase of over 50% compared to such procedures initiated during the previous two-year period, 2007-2008 (totaling 24). As a result of the proliferation of international disputes to resolve cases of double taxation, as well as recent developments in legislation and interpretation concerning this subject, the need has emerged for the Italian tax authorities to issue some guidance on the management of tax disputes under MAPs, for taxpayers to use, as well as by the peripheral offices (regional and provincial) of the same tax authorities which are required to support the Department of Finance (Ministry of Economy and Finance) from preliminary preparatory activities to the conducting of the procedure and right up until the final decision stage. These guidelines have been collected in Circular 21/E of 5 June 2012 (Circular 21), which deals, in particular, with the resolution of disputes in the more general scope of bilateral income tax treaties pursuant to article 25 of the OECD Model, and, more specifically, to the rules laid down by the Arbitration Convention (90/436) of 23 July 1990, agreed between the EU Member States with the purpose of amicably settling disputes on transfer pricing between associated enterprises.

In addition to a broad overview of the subjective and objective requirements for a taxable person resident in Italy to access procedures, as well as the procedural steps related to the two different procedures in order to outline which ones comply with international best practices, the tax authorities have focused on some important aspects which previously had not been clarified, concerning the links with domestic law, and, more specifically, with domestic disputes, collection of any additional taxes or sanctions, and with the so-called "deflationary instruments of litigation". These latter aspects will be dealt with in this article, bearing in mind that while the MAP provided for under article 25 of the OECD Model (2010) may cover all cases generating legal and economic double taxation in contrast with bilateral income tax treaties, the Arbitration Convention (90/436) refers only to cases of double taxation of profits in transactions between associated enterprises resident in the European Union.

Circular 21 clarifies that the situations subject to the Arbitration Convention (90/436) include only those adjustments made in application of article 110, paragraph 7 of Presidential Decree 917 of 22 December 1986 and not those increases based on the absence of relevance of 3. The Italian tax authorities note that practices for the avoidance or removal of double taxation in cross-border transactions between enterprises belonging to the same group are also dealt with in Chapter IV of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administration (2010) (OECD Guidelines), International Organizations' Documentation (IBFD) which mentions, among the recommended paths for non-adversarial settlement, the MAP referred to in article 25 of the OECD Model (2010). Circular 21, however, makes no reference to the further bilateral process codified in article 9(2) of the OECD Model (2010), namely the corresponding adjustment under which, with regard to transfer pricing, a contracting state may grant a downward adjustment of the taxable income of an associated enterprise in order to balance, at the group level, the effect generated by a corresponding increase implemented in another state.


5. Pursuant to article 110, paragraph 7 ("The income components of transactions with non-resident enterprises which directly or indirectly control the company, or which control or are controlled by the same enterprise that controls the company, are evaluated based on the normal value of the goods and services offered, or the goods and services received, as established under para. 2 (art. 110), if there is an increase in income, the same provision is also applied if there is a decrease in income, but only in compliance with the terms of agreements with the authorities of the foreign country in line with the special "mutual

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costs incurred between the enterprises of the same group (article 109, paragraph 5 of Presidential Decree 917 of 22 December 1986). 

2. Relationship with Domestic Disputes and Identification of “Serious Penalties” under the EU Arbitration Convention

In Circular 21, the tax authorities examine the relationship between domestic judicial proceedings and the amicable settlement between states separately for each of the two procedures, due to their differing natures. They take into account, however, a commonly applied principle under which it is understood that, whatever the outcome of a MAP, where domestic judicial proceedings have run their course, the Italian tax authorities may not object to, derogate from or act in a manner contrary to the decision of the judicial body.

2.1. Bilateral income tax treaties: article 25 of the OECD Model

Paragraph 1 of article 25 of the OECD Model provides that any taxpayer that believes that double taxation has or may occur contrary to the provisions of the treaty, may request the activation of a MAP to remedy this situation, regardless of the procedures prescribed by the national legislation of the contracting states. Until 2008, a taxpayer that requested the activation of a MAP had to rely on the goodwill and diligence of the competent authorities to reach a satisfactory result, as there was no obligation for the tax authorities of the two contracting states to produce a result that would effectively remedy the situation.

With the insertion of the new paragraph 5 in article 25 in July 2008, the possibility opened for a taxpayer to request, in cases where the competent authorities of the states involved in a MAP do not reach an agreement within two years, that the matter be resolved through recourse to independent arbitration.

The introduction of paragraph 5, according to the Commentary on Article 25 of the OECD Model,1 has the primary purpose of increasing the actual success of the resolution of disputes with a MAP (with paragraph 5 representing the final stage) through independent decisions that are binding on the contracting states. However, its application and effectiveness depend on the compatibility of arbitration with the domestic rules of each state and on the binding nature of an arbitration decision. For this reason, each state may decide to introduce in its bilateral income tax treaties paragraph 5 in its standard treaty formulation or to include paragraph 5 but limiting its application to certain specific cases.

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1. Agreement procedures provided for under bilateral income tax treaties (author's translation).
2. Under article 109, paragraph 5, costs and other negative elements other than interest payable [...] are deductible if and to the extent that they refer to assets or property from which derive revenue or other income that would form income or would not as they are excluded.
4. The meaning of “deflationary instruments” is here “administrative instruments aimed at the limiting or lowering of penalties.”

No recently concluded (after July 2008) Italian bilateral income tax treaty contains or has been modified to contain an arbitration clause in accordance with paragraph 5, as the Italian tax authorities note in Circular 21. Only some Italian treaties, referred to in the Circular, including that with the United States, provide for the possibility, under particular conditions, of submitting a case for binding arbitration with the consent of both contracting states and the taxpayer concerned. Therefore, in all other cases of bilateral income tax treaties that do not include an arbitration clause, a taxpayer resident in Italy which complains of double taxation and which has carried out a MAP to no avail in accordance with paragraph 1 of article 25, is currently unable to resort to arbitration.

In this context, where (1) the activation of the MAP does not interrupt the time period specified under domestic law to access national courts or “deflationary instruments” in the event of objections from the tax authorities and (2) above all, the use of a MAP, save for a few exceptions, does not guarantee that a result will be reached and does not bind the national authorities to observe the decisions of independent arbitration, if in Italy notices have already been served or measures have been taken that cause an increased tax liability for the taxpayer, to start, alongside the MAP, a domestic proceeding too is a particularly appropriate, although unnecessary action (Circular 21, paragraph 4.2.5). It is appropriate (or, more correctly, necessary) to refer the matter to the national court because, where an increased tax liability is determined and such determination becomes definitive owing to the expiration of the statute of limitations for filing an appeal with the tax court and no decision has been agreed by the competent authorities as a result of the MAP, the taxpayer would have no other forum to argue the case and would remain affected by the double taxation.

The concurrence of domestic judicial proceedings with a MAP may lead to the following consequences, depending on whether the agreement between the contracting states, if reached, occurs before or after the judge’s decision:

- in the former case, the execution of the MAP will take place following the waiver of the domestic action by the taxpayer; or
- in the latter case, should the mutually agreed solution be in conflict with the judgement, the Italian tax authorities may not lawfully adopt any agreement concluded with the other contracting state in favour of the taxpayer as part of a MAP. In this situation, the removal of the double taxation may take place only if the foreign tax authorities so desire.

It remains possible for a taxpayer to request that the tax court suspend any decision pending the conduct of the MAP in order to know the outcome before the conclusion of the proceedings.

Similarly, a taxpayer may resort to ordinary domestic procedures to obtain, either administratively or judicially, the

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8. The meaning of “deflationary instruments” is here “administrative instruments aimed at the limiting or lowering of penalties.”
benefit of the suspension of collection of the additional taxes and the related penalties temporarily imposed.

2.2. EU Arbitration Convention

2.2.1. Generally

The scenario is different when a case of double taxation can be remedied by resorting to the Arbitration Convention (90/436). In these cases, the states involved are required to reach an agreement by means of a MAP, or should the MAP be ineffective, by resorting to arbitration (article 7, paragraph 1). A taxpayer, therefore, having activated the MAP in accordance with the Arbitration Convention (90/436), has the assurance that the tax authorities of the states involved, either independently or with the help of an ad hoc commission, will seek a joint solution.

However, the choice of the path of international dispute resolution for an Italian taxpaying enterprise is limited by the principle mentioned above, whereby an arbitration decision may not in any case derogate from a judgment issued by a domestic court. For Italy, paragraph 3 of article 7 of the OECD Model is applicable, which provides that:

where the domestic law of a Contracting State does not permit the competent authorities of that State to derogate from the decisions of their judicial bodies, paragraph 1 shall not apply unless the associated enterprise of that State has allowed the time provided for appeal to expire, or has withdrawn any such appeal before a decision has been delivered.

The resident taxpaying enterprise generally may both activate the treaty-based MAP and rely on the national tax court. However, in the case where no amicable solution is found, recourse to the arbitration commission is precluded if the same enterprise does not waive its right to appeal against the Italian tax authorities before the tax court.

In any case, the Arbitration Convention-based path may no longer be taken when the national tax court has delivered its first judgment.

If, once a national proceeding has been initiated, a decision has been given by the court, and if no elimination of double taxation has resulted therefrom, the court’s decision will remain in place until the foreign competent authority remedies it by adapting its work to comply with the decision of the Italian court.

With regard to the collection of additional taxes and related sanctions assessed on a provisional basis, pending an arbitration proceeding, the domestic law ratifying the Arbitration Convention (90/436) contains a special provision that states that the Italian tax authorities may order the suspension in accordance with the purpose of the arbitration in process. Circular 21 naturally specifies that the specific remedy referred to in the ratifying law may be activated only if the taxpayer has already waived its right to domestic litigation, as an alternative to the request for suspension provided by the tax process.

2.2.2. Serious penalties

A further limitation on accessing EU conciliation procedures is contained in the Arbitration Convention (90/436), which provides that a MAP (article 6) or arbitration procedure (article 7) may be suspended when the enterprise concerned must pay “serious penalties” in accordance with a concurrent judicial procedure or domestic administrative procedure. With regard to the identification of serious penalties, accepting suggestions in this regard that have emerged from the Joint Transfer Pricing Forum, as well as integrating the Code of Conduct for the application of the Arbitration Convention (90/436), the EU Council of Ministers has stated: “Member States are recommended to clarify or revise their unilateral declarations in the Annex to the Arbitration Convention (90/436) in order to better reflect that a serious penalty should only be applied in exceptional cases like fraud.”

Italy had already expressed its position, which complies with the following recommendation, in the Italian enactment of the Arbitration Convention (90/436), stating: “The term ‘serious penalties’ means penalties laid down for illicit acts, within the meaning of the domestic law, constituting a tax offence.”

Circular 21 aims to clarify and limit the cases of tax offenses that may constitute an obstacle for the continuation of a MAP or arbitration. Italy has chosen to limit the field of relief referred to in article 8 of the Arbitration Convention (90/436) to tax offenses of a criminal nature, without extending it to the field of administrative penalties.

Cases involving the following crimes are precluded from seeking relief under the Arbitration Convention (90/436):
- a fraudulent tax return deriving from the use of invoices or other documents relating to non-existent transactions (article 2 of Legislative Decree 74 of 10 March 2000); and
- a fraudulent tax return deriving from the use of other means (article 3 of Legislative Decree 74 of 10 March 2000).

The tax authorities emphasize that in the case of such offenses, the breach is not generated by a problem in the evaluation of the transactions between associated enterprises under the principle of the free market, but rather originates from actions or false or forged documents in order to conceal material facts that actually or otherwise occurred. In other words, the criminal offense is pre-existing and prevalent with regard to any defect of evaluation of transfer prices within the group.

The case of criminal risk connected with the offense of lodging an untrue tax return is different (article 4 of Legislative Decree 74 of 10 March 2000). Under this provision, a violation involving the lodging of an untrue tax

11. Arbitration Convention (90/436) – Unilateral Declaration on Article 7 – Italy – “The term ‘serious penalties’ means penalties laid down for illicit acts, within the meaning of the domestic law, constituting a tax offence.”
return, which is a considerable violation for criminal purposes, occurs if the increases in declared income discovered by the tax authorities exceed the value limits provided under this provision. However, the criminal characterization may no longer be applied if the taxpayer's conduct indicates no deliberate intent to defraud the tax authorities. Therefore, a variation (increase) in the taxable amount deriving from the revision of the method of evaluating transfer prices between associate enterprises may occur, which would entail, given the amount, the offense of lodging an untrue tax return. Circular 21 clarifies, however, that such violation would be punishable under criminal law and consequently would result in the suspension of a MAP or arbitration only if, during the process of evaluating the transfer prices, the taxpayer is found to have been deliberately evasive.

3. Relationship with “Deflationary Instruments of Litigation”

The Italian legal system provides certain legal processes - so-called "deflationary instruments of litigation" (settlement of tax assessment, tax mediation and settlement in court) - which the taxpayer and the tax authorities may (or should) use to attempt to reach an out-of-court resolution to a dispute arising from a proposed increase to tax liability, prior to the involvement of a judicial authority or pending the tax proceeding. At the national level, if a dispute is resolved through the application of one of these legal processes, the defining decision is binding on both of the subjects involved (the taxpayer and the tax authorities) and, except in specific cases, may not be revised. If, however, a resolution is not agreed under one of these legal processes, there would continue to be a possibility of referring the case to the tax court (or such a possibility would arise).

3.1. Bilateral income tax treaties: article 25 of the OECD Model

With regard to the activation of a MAP pursuant to article 25(1) of the OECD Model, the access to a deflationary legal process and the resulting resolution by means of an agreement between the taxpayer and the tax authorities, renders any resolution regarding the same case agreed between the tax authorities of the two states involved ineffective. In other words, should the tax authorities and the taxpayer reach an agreement with regard to the case of alleged double taxation, this understanding may not be modified and is consolidated while the MAP is still in progress and independently of the result of the MAP. This is also the case if the domestic agreement reached under a deflationary process does not have the effect of eliminating the original double taxation entirely; in which case the only possible remedy is the substantially unilateral discretion of the foreign authorities to confirm their position in order to eliminate the double taxation.

3.2. EU Arbitration Convention

Albeit for different reasons arising from the substantially different nature of the two procedures, both the principle of unmodifiability of agreements reached under the deflationary acts of defining the domestic dispute and the effects of such agreements on the result of the non-adversarial procedure governed by article 25 of the OECD Model are, according to the opinion expressed by Circular 21, equally valid with respect to the procedure for resolving disputes as provided under the Arbitration Convention (90/436).

The use of a deflationary process is an explicit expression of the desire to define the relationship between taxpayers and the tax authorities without resorting to national or international (EU) litigation. Therefore, an agreement reached at the conclusion of the deflationary process precludes any effect of an intervening arbitration decision in application of the Arbitration Convention (90/436).

If the double taxation has not been fully removed by means of the deflationary process, in this case too it remains possible to achieve the elimination of the double taxation through the unilateral intervention of the foreign tax authority during a MAP.
Circular 21/E

Resolution of International Taxation Disputes – Mutual Agreement Procedures

Central Assessment Office
Rome, 5 June 2012

Preamble

The last three years have seen a gradual and conspicuous increase in international disputes connected with mutual agreement procedures established in order to address cases of double taxation.

The commitment of the Tax Authorities [Agenzia delle Entrate] has therefore increased with regard to the consultancy and support provided to the Department of Finance – the institutional reference for the political/negotiation management of mutual agreement procedures – with the aim of defining Italy’s position with regard to foreign counterparts.

In this context the involvement of the Agency’s regional and provincial offices shall be of primary importance, in terms of sharing practices and participation in the preliminary investigation activities for the conducting of the international dispute resolution process and its success.

In order to ensure that administrative action is adequately consistent with the principles stated by international reference sources, this Circular provides clarification with regard to the management of tax disputes under a mutual agreement procedure (hereinafter referred to as "MAP").

In particular, the various characteristics of the procedure are illustrated according to legal grounds for the initiation thereof that can be traced to conventions for the avoidance of double taxation in force between Italy and the contracting states of the treaties (hereinafter referred to as "bilateral conventions") and, at EU level, to Convention 90/436/ EEC of 23 July 2990 on the elimination of double taxation in connection with the adjustment of profits of associated enterprises (hereinafter referred to as the "Arbitration Convention").

The various stages of the procedure and their respective connections with domestic law are also explained. Lastly, a precise guide is also provided with regard to the subjective and objective requirements for eligibility, as well as the methods by which a MAP may be accessed.

Please note that cases of double taxation arising from the adjustment of profits of associated enterprises, in applica-

ation of transfer pricing legislation, are some of the most common situations that are subject to a mutual agreement procedure. This is due to the fact that evaluations of actual compliance with the conditions of free competition in connection with transactions between associated enterprises are characterized by particular complexity and technicality.

It follows that, notwithstanding the applicability of this Circular to all cases governed by the relevant supranational provisions, the indications contained herein are concentrated particularly on the principal problematic issues connected with the mutual agreement procedures that are initiated following transfer price adjustments.

1. International Juridical Foundations

As mentioned in the introduction, the international reference sources are bilateral conventions for the avoidance of double taxation and the Arbitration Convention.

Bilateral conventions, as well as containing specific provisions for the removal or mitigation primarily of the phenomena of international double taxation, envisage a specific instrument for resolving any disputes that may arise between the states: the mutual agreement procedure governed by article 25 of the OECD Model Convention for the Avoidance of Double Taxation on Income or on Capital (hereinafter the "OECD Model") and its related Commentary.²

The mutual agreement procedure was established as a direct consultation between the tax administrations of the contracting states, which communicate via their "competent authorities", in the manner considered most appropriate, with a view to reaching an agreement on the subject of the procedure. In this sense a MAP is an instrument for resolving international disputes in situations where a resident of one of the two contracting states considers that the measures adopted by one or both tax authorities result or will result in a tax which does not comply with the provisions of that convention.

1. Reference is made, in particular, to the rules governed in the Italian tax system by article 110, section 7 of the Consolidated Income Tax Act, approved by Presidential Decree 917 of 22 December 1986 and applicable to transactions between companies, enterprises, permanent establishments and bodies belonging to the same multinational group, as well as the provisions contained in Articles 7 and 9 of bilateral conventions and in article 6 of the Arbitration Convention.

2. OECD Committee on Fiscal Affairs, Model Tax Convention on Income and on Capital (as read on 22 July 2010).
Italy has signed a large number of bilateral conventions with the objective of eliminating juridical and economic double taxation by means of the allocation of taxing rights between contracting states. Each one includes a provision equivalent to article 25 of the OECD Model Tax Convention, concerning mutual agreement procedures.

In order to facilitate a more effective and transparent management of MAPs, in 2004 the OECD initiated an ongoing project aimed at improving the operation of mechanisms for the resolution of international tax disputes. This project led, among other things, to the drafting of the OECD Manual on Effective Mutual Agreement Procedures (hereinafter referred to as “MEMAP”). The latter provides tax authorities and taxpayers with basic information on the operation of MAPs and identifies some best practices with which the tax authorities of Member countries should comply.

Even the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, in Chapter IV on the administrative approaches to avoiding and resolving disputes resulting from transfer pricing adjustments, contain a special section dedicated to the use of MAPs. It addresses both general issues and those most closely connected with the problem of corresponding adjustments to be carried out in the event of primary transfer pricing adjustments.

In addition to bilateral conventions, the Arbitration Convention mentioned above is also in force and may be accessed in the event of economic double taxation resulting from transfer pricing adjustments applied between associated enterprises resident in the European Union.

For purposes of the application of the Arbitration Convention, reference must also be made to the recommendations contained in the “Code of Conduct for the effective implementation of the Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises” adopted by the Council of the European Union on 22 December 2009 (hereinafter referred to as the “Code of Conduct”).

2. Domestic Juridical Foundations

With regard to the domestic regulatory framework, the juridical foundation for the establishment of a mutual agreement procedure is found in the individual bilateral conventions signed by Italy, all ratified by law, and in the Arbitration Convention, ratified by Law 99 of 22 March 1993.

Moreover, the Italian tax system contains an express reference to mutual agreement procedures in paragraph 7, second sentence of article 110 (General Rules on Evaluations) of the Consolidated Income Tax Act 917 of 22 December 1986, wherein it is stated that the rules for the determination of the normal value also apply even if a decrease in income results, but only in the execution of agreements concluded with the competent authorities of foreign States as a result of special mutual agreement procedures provided for by international conventions for the avoidance of double taxation of income. The aforementioned provision confirms, in particular, the correlation between transfer pricing and the international treaty regulation of double taxation.

3. Institutional Actors

The bodies that govern the management and handling of mutual agreement procedures are the Ministry of the Economy and Finance – Department of Finance (as the competent authority for Italy) and the Revenue Agency.

In general, the term “competent authority” means that body which represents a contracting state in the relations arising from a treaty. With specific reference to MAPs, the competent authority is the body that exercises the functions of representing the state for all matters concerning the internal (domestic) aspects of the dealings with the taxpayer and the external (foreign) aspects concerning dealings with the other state involved in the procedure.

The competent authority endeavours to guarantee the application of the Convention in good faith, negotiating solutions inspired by principles of fairness and transparency with the other contracting state.

The Revenue Agency therefore provides the Italian competent authority with the technical support and the necessary collaboration during the course of the whole MAP activity, interacting in particular during the stage relating to the drafting of the position paper and the corresponding exchange of papers which are instrumental in illustrating, to the competent authority of the other state, the factual and legal basis of the case under consideration. The role of the Revenue Agency also takes on significance in view of the need to ensure the maximum consistency between the technical positions taken during the procedure and those expressed in other contexts, specifically during the interpretation, control and prevention of disputes.

3. Juridical double taxation is the imposition of taxation in two or more contracting states on the same taxpayer with regard to the same income component (such as dividends or interest). Economic double taxation, however, is the imposition of taxation in two or more contracting states on two or more taxpayers with regard to the same income component (for example the profits of associated enterprises). See Commentary on art. 23 A and B of the OECD Model Tax Convention, paragraphs 1 and 2.


5. Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, the revised and integrated text of which was approved by the OECD Council on 22 July 2010.


7. An updated list of bilateral conventions is available on the website of the Department of Finance, www.finance.it.


9. A position paper refers to the document in which the Tax Authority indicates the technical and legal reasons justifying its position.

10. With regard to the prevention of disputes, particular reference is made to the procedure of the “international standard ruling,” introduced in the Italian
4. Article 25 of the OECD Model

As mentioned, all bilateral conventions entered into by Italy contain a founding clause, corresponding to article 25 of the OECD Model, on mutual agreement procedures.

The procedure is structured firstly pursuant to paragraphs 1 and 2 of article 25, as a remedy available for a taxpayer who claims to be or could be suffering from a tax which is not in accordance with the convention.

Furthermore, pursuant to paragraph 3 of article 25, it is possible for a mutual agreement procedure to be initiated directly by the competent authorities of the contracting states.

The two cases are analysed separately.

4.1. Mutual agreement procedures initiated by competent authorities

The first part of paragraph 3 of article 25 of the OECD Model provides that the mutual agreement procedure may also be initiated by the contracting states' competent authorities in order to resolve the difficulties or doubts concerning the interpretation of application of the Convention by mutual agreement.

These are essentially difficulties of a general nature, that concern specific categories rather than individual taxpayers, even though such difficulties may have been highlighted in relation to individual cases covered by paragraphs 1 and 2 of article 25.

Furthermore, pursuant to the second part of paragraph 3, the two Authorities may consult together in order to eliminate double taxation in cases not provided for in the Convention. For example an enterprise resident in a third state with permanent establishments in both contracting states comes under this latter case.

Consequently, alongside a mutual agreement procedure designed to resolve specific instances of taxation contrary to the provisions of the convention, the possibility is identified that a mutual agreement procedure may be commenced at the instigation of the competent authorities in order to resolve issues related to the interpretation or application of the convention or to resolve situations not covered by the convention.

The agreement reached by the competent authorities under a mutual agreement procedure initiated pursuant to article 25, paragraph 3 of the OECD Model, affects a large number of taxpayers and, therefore, should be adequately publicized.

4.2. Mutual agreement procedures initiated at the instigation of the taxpayer

4.2.1. Subjective scope

Article 25, paragraph 1 of the OECD Model provides that if a "person" considers that a tax that is not in accordance with the Convention has been or could be levied against him, he may present his case to the competent authority of the state he is resident of, or, if his case comes under paragraph 1 of article 24 (Non-Discrimination) of the same OECD Model, to the competent authority of the state of which he is a national.

It must be highlighted that not all bilateral conventions signed by Italy contain a reference to nationality alongside the reference to residence. It follows that, in this case, should the taxpayer intend to make use of the principle of non-discrimination, he should refer directly to the individual bilateral conventions signed by Italy with the foreign state concerned, in order to establish whether or not he is entitled to initiate a mutual agreement procedure.

The term "person" includes individuals, corporations, companies and any other association or entity possessing tax liability and resident, for tax purposes, in the territory of one of the two contracting states to the convention.

Furthermore, double taxation does not necessarily have to have already occurred; it is sufficient, for the purposes of an interested party's claim, that the same party believes that the tax measures imposed on it will lead to this effect.

4.2.2. Objective scope

The provision contained in article 25, paragraphs 1 and 2 of the OECD Model includes all those cases generating juridical or economic double taxation that affect both individuals as well as legal persons and other entities to which the Convention applies.

For individuals, it could be a case of dual tax residence, incorrect application of withholding tax on dividends, interests and royalties or a disputed classification of income from employment received by the taxpayer etc.

With reference to persons other than individuals, the procedure may involve issues such as the existence of a permanent establishment, the correct allocation of profits to the associated enterprises of a multinational group, the qualification of incomes as business profits or as a different category governed by specific convention provisions etc.

4.2.3. Time limits for submitting a MAP request

For the correct identification of the time limit within which a taxpayer may request the initiation of a mutual agreement procedure, reference must be made to that provided in the individual bilateral convention applicable to the case at hand.

Indeed, although the OECD Model identifies as the final date for the presentation of a request the third year from the first notification of the action resulting in taxation not in accordance with the provisions of the convention, the
majority of bilateral conventions signed by Italy identify a shorter term (generally two years).

Moreover, for purposes of calculating the starting point of the limitation period, the term "first notification of the action resulting in taxation not in accordance with the provisions of the Convention" should be interpreted in the way most favourable to the taxpayer, according to the interpretation contained in paragraph 21 of the Commentary on article 25 of the OECD Model.

It is therefore necessary to distinguish between (i) the situation in which a taxpayer claims that the charge resulting from the application of a domestic tax or domestic withholding tax is not in accordance with the provisions of the Convention (for example withholding tax applied to payments of dividends, interest and royalties) and (ii) the situation in which the such levying results from adjustments made by the Tax Authorities (for example, objections or adjustments transfer prices applied to transactions between associated enterprises).

In case (i), the time limit for the valid presentation of a request to initiate a MAP begins from the date of notification by the Tax Authority denying the requested refund with regard to the withholding tax levied, which runs from the ninetieth day after the presentation of the refund request without having received the decision of the Tax Authority, in accordance with the provisions of article 37, second paragraph, and article 38 of Presidential Decree 602 of 29 September 1973. 11

In case (ii), consistent with the position expressed by Italy in its compliance with the Code of Conduct for the effective implementation of the Arbitration Convention, the starting date for the period within which the taxpayer must present the request coincides – also for purposes of a bilateral MAP – with the date of notification of the assessment that generated the tax not in accordance with the convention.

It must be stated that the taxpayer may submit the request prior to the notification of a formal notice of assessment. For example, it is possible to request the initiation of a mutual agreement procedure following the notification of an official report on the findings. In this case, the mutual agreement procedure is commenced to commence from the date on which the competent authority receives the request and the minimum information necessary in order for the procedure to be instituted.

4.2.4. Content and manner of submitting a MAP request

In principle, the request for a mutual agreement procedure must be submitted directly by taxpayers in their country of residence.

However, with regard to transfer pricing adjustments, a mutual agreement procedure request is, as a rule, submitted in the state that enacted the law that gives rise to the double taxation, by the resident enterprise that is the subject of assessment. That being said, with regard to such cases a mutual agreement procedure may still be validly established by the associated foreign enterprise when the amount subject to adjustment in the former state has already been subject to taxation. In this case, the associated enterprise applies to the competent authority of its own state of residence to object to the double taxation arising within the multinational group.

It should be noted that in addition to persons who are assigned as representatives of taxpayers other than individuals, the procedure may be initiated also by a taxpayer's attorney vested with general or special authority. In this case, the power of attorney must be granted in accordance with the formalities specified under article 63 of Presidential Decree 602 of 1973.

In the case of a MAP initiated by a person resident in Italy, the application must be drafted on plain paper and sent by registered mail with an acknowledgement of receipt to the Ministry of Economy and Finance, Department of Finance – International Relations, or hand delivered to the same department along with a copy of the first page of the application for the department's stamp and date stamp attesting delivery (and receipt) of the application. It is possible – and also appropriate in the event that the case involves a substantial amount of material – to provide documentation supporting the application in electronic form.

Submission of an application to initiate a mutual agreement procedure is not subject to any kind of fee.

In order to expedite the evaluation process and the subsequent instigation of contacts with the foreign competent authority, the application should preferably contain the following information:

1. taxpayer identification (name, address and tax identification number);
2. indication of the domicile of the taxpayer or the domiciliary to whom the tax administration may address its communications;
3. explanation of the facts and circumstances of the case, and indication of the tax periods in which the double taxation occurred or could occur;
4. description of any administrative and/or jurisdictional actions filed in Italy, such as the filing of a tax settlement proposal or judicial appeal;
5. any remedies implemented in the other contracting state in order to eliminate double taxation;
6. a copy of the tax documents that have resulted or could result in a tax which is not in accordance with the provisions contained in the bilateral convention (in particular, where appropriate, a copy of the express decision denying a tax refund or, in the case of fact denial, a copy of the refund request filed in accordance with article 37, second paragraph, or article 38 of Presidential Decree 602 of 1973); and
7. any additional supporting documentation which would assist the preliminary work of the competent authorities concerned with the mutual agreement procedure.

11. In this regard, it must be borne in mind that non-residents are obliged to contact the Operations Centre in Pescara.
The request must also contain the taxpayer's undertakings to respond fully and promptly to the requests of the competent authority during the mutual agreement procedure and to make any additional documentation available which may be necessary for the procedure.

However, particularly with regard to MAPs resulting from transfer pricing adjustments, reference should be made to the guidance provided in section 5.5., below, concerning the initiation of a mutual agreement procedure in accordance with the Arbitration Convention.

4.2.5. Relationship with domestic legal proceedings

Article 25, paragraph 1 of the OECD Model provides that a mutual agreement procedure may be requested by a taxpayer "irrespective of the remedies provided by the domestic law [...]". In this regard, the majority of the conventions signed by Italy contain, in the related accompanying Protocol, a provision on the interpretation of the MAP article under which the phrase "irrespective of the remedies provided by the domestic law [...]" is understood to mean that "the mutual agreement procedure is not an alternative to domestic dispute proceedings which, in any case, are initiated in advance should the dispute concern the application of taxes not in accordance with the Convention" (or an equivalent thereto).

In general, MAPs initiated in Italy in accordance with a bilateral convention are accompanied by a judicial proceeding brought pursuant to domestic law. The opportunity to appeal to the Tax Court corresponds to the need to avoid, during a mutual agreement procedure, the tax imposed in Italy becoming final and, therefore, irrevocable in spite of any agreement reached between the competent authorities.

Moreover, the simultaneous execution of a mutual agreement procedure and domestic judicial proceeding leaves open the possibility of a ruling that conflicts with any mutual agreement reached between the competent authorities. In this case, the Tax Authority could find itself in the position of not being able to legitimately fulfill its international obligation as undertaken under the mutual agreement.

Consequently, should the competent authorities reach an agreement that eliminates the double taxation without a final judicial judgement having been rendered, a prerequisite for the execution of the mutual agreement is the acceptance of its contents by the taxpayer and the simultaneous waiver of the judicial appeal.

In the reverse case where a judgement has been given before a mutual agreement has been reached, the Italian competent authority must merely notify the final outcome of the proceedings to the other competent authority. In this case, if the judgement does not eliminate the double taxation, the latter shall remain, unless the foreign competent authority conforms its position to the decision expressed by the domestic court.

Moreover, it is up to the taxpayer to decide whether he will propose a suspension of legal proceedings pending the execution of the mutual agreement procedure. In this latter regard, recent experience has seen more than one case where a suspension had been granted by the Tax Court pending a decision by the competent authorities. Of course, in the event that no agreement is reached by the competent authorities, a request will be made for a continuation of the domestic proceedings which had been suspended when the MAP was initiated.

Lastly, it should be noted that in the event of an adjustment effected in the other contracting state, any pending dispute abroad shall not constitute grounds to prohibit the initiation and continuation of a mutual agreement procedure, provided that the other tax authority demonstrates the same willingness.

4.2.6. Arbitration clause

A distinctive feature of a mutual agreement procedure initiated pursuant to a bilateral convention is that the competent authorities are not obliged to find a remedy to ensure the elimination of the reported double taxation. There is only the duty of diligence, which requires that the tax authorities concerned "endeavour" to reach an agreement that eliminates the taxation not in accordance with the convention.

In this regard, the OECD Commentary on article 25 (paragraph 37) expressly clarifies that "Paragraph 2 no doubt entails a duty to negotiate; but as far as reaching mutual agreement through the procedure is concerned, the competent authorities are under a duty merely to use their best endeavours and not to achieve a result."

In practice, it may therefore occur that the issue referred to the competent authorities of the contracting states will not be resolved.

It is worthwhile recalling the amendment introduced in 2008 to article 25 of the OECD Model, which now provides, in paragraph 5, for a mandatory arbitration phase should a mutual agreement not be reached within two years by the two states that are party to the mutual agreement procedure.

The new paragraph 5 of article 25 is applicable provided that, at a bilateral level, its insertion is negotiated (or renegotiated) into a new (or existing) convention to avoid double taxation. Much depends on the willingness of the states to negotiate, and they may prefer to introduce such a clause in the Conventions entered into with some partner states rather than others, based on different kinds of assessments.

Certainly, when there is a bilateral convention that includes a clause corresponding to paragraph 5 of article 25, the efficacy of the mutual agreement procedure is strengthened.

It should be noted that, at present, thirteen conventions in force between Italy and partner states contain an arbitration clause. This clause, found in Conventions negotiated...
before the insertion of the arbitration clause in the OECD Model, typically provides for the initiation of arbitration only after the consent of both states and the taxpayer has been obtained. It therefore does not set forth a preventive constraint (mandatory arbitration) for the contracting states to undertake arbitration in the event of a failure to resolve the dispute by mutual agreement. In some cases, the clause's effectiveness is also subject to the condition that an exchange of information have previously taken place between the states. The exchange of information, in addition to expressing the intention of the states to implement the arbitration clause, is intended to define the relevant operational terms (manner of formation of the advisory commission, member selection criteria, cost allocation, choice of language, etc).

4.2.7. Suspension of tax collection

In this regard, ad hoc remedies for mutual agreement procedures initiated on the basis of bilateral conventions are not provided for, without prejudice to the possibility for the taxpayer to benefit from ordinary measures – such as the administrative or judicial provision for the suspension of tax collection – provided by article 39, paragraph 1 of Presidential Decree 602 of 1973 and article 47 of Legislative Decree 546 of 31 December 1992 respectively.

4.2.8. How the procedure is conducted

Article 25, paragraph 2 of the OECD Model provides that, should the competent authority consider the claim made by its taxpayer as justified, but is unable to independently reach a satisfactory solution, the competent authority must endeavour to resolve the case by way of mutual agreement with the competent authority of the other state. It is therefore possible to distinguish two stages in the mutual agreement procedure.

In the first stage, the competent authority that receives the claim must rule on its admissibility. To this end, it must assess whether the objective and subjective requirements exist for the initiation of a mutual agreement procedure and it must ascertain, in particular, whether the claimant correctly deems that the actions of one or both states result or will result in a taxation which is not in accordance with the convention. Where the mutual agreement procedure concerns the refunding of taxes levied in breach of the provisions of the convention, assessment of the admissibility of the claim – including verification of the valid submission of the request for refund and receipt of a denial or expiry of the time limit provided for the deemed existence of tacit denial – is carried out together with the Revenue Agency.

If the claim is found to be admissible and well founded, the competent authority should consider the opportunity to remedy such claim through the adoption of unilateral measures only with regard to the taxation which is not in accordance with the convention. If not, notice of the claim by the taxpayer is given to the competent authority of the other state for an assessment at a higher level.

In accordance with the above, once the Department of Finance of the Ministry of Economy and Finance has received the claim, it shall assess its admissibility in terms of whether it meets the subjective and objective requirements outlined in the previous points regarding access to the procedure, resorting – if necessary – to the Revenue Agency for its opinion on any uncertain issues.

At this stage, the competent authority may also request that the taxpayer produce additional information and supplementary documentation necessary for the initiation and execution of a mutual agreement procedure. Where the taxpayer has not already done so, the competent authority or, where appropriate, through the foreign competent authority, will request that the taxpayer submit a claim for a tax refund in accordance with article 37 or 38 of Presidential Decree 602 of 1973.

Lastly, the competent authority shall inform the claimant as to whether the claim is admissible and whether the procedure has been validly established.

If the double taxation arises from an act of the Revenue Agency, the latter shall assess whether, prima facie, the discernible elements exist which would lead to the elimination of the double taxation by means of a unilateral act, namely by its own determination in accordance with Decree-Law 564 of 30 September 1994, ratified, with amendments, by Law 656 of 30 November 1994. Similarly, if the double taxation arises from an act of the Foreign Administration, the Revenue Agency shall assess the possibility of granting a tax refund or tax relief to the resident taxpayer, in consideration of the manifest conformity of the foreign action to the applicable provision of the convention.

If, however, a unilateral elimination of the double taxation is not considered feasible, the Italian competent authority shall inform the authority of the other state about the decision to initiate a MAP; the Revenue Agency shall be informed at the same time.

The date the MAP is initiated coincides with the original date of submitting the request and the attached documentation, unless it is necessary to submit additional documentation. In the latter case, the procedure commences from the date such documentation is submitted.

If the MAP request is submitted by an affiliated person in the other state involved in the procedure (cases of transfer pricing adjustment), the relevant date shall be communicated promptly by the foreign competent authority.

With reference to the execution of the mutual agreement procedure initiated in accordance with a bilateral convention, the Italian Tax Authority shall conform, to the extent possible, to the temporal and procedural guidance contained in the Code of Conduct for the effective implementation of the Arbitration Convention. In this regard, reference is made to the table in section 5.8. of this Circular.
Dealings between the competent authorities aimed at resolving a case of double taxation normally take place via an exchange of position papers (in writing) and, where necessary, the scheduling of meetings for negotiations. As a rule, the competent authority that sends its own position paper first is that of the state that adopted the measure likely to result in double taxation. In general, the English language is used in the drafting of the position papers.

4.2.9. Role of the taxpayer

The mutual agreement procedure is a means of resolving disputes between contracting states in the exercise of their powers of taxation. The sole interlocutors during the procedure are the competent authorities of the two states, and they are the only two parties entitled to sign any bilateral agreement that may be reached.

The above does not exclude the possibility that the taxpayer will still be invited to play an active role, particularly with reference to the need to describe the case promptly and truthfully, providing any information which would ensure that the matter is dealt with exhaustively. In this regard, the taxpayer must, as a rule, be cooperative and transparent, and act in good faith.

On the other hand, the taxpayer is also granted the right to information. In particular, the MEMAP (Section 3.3.3. and concerning Best Practice 14) recommends that the taxpayer be informed on the status of the procedure by the competent authority and that the taxpayer may request to be heard concerning the dispute.

In the case of a mutual agreement procedure arising from a transfer pricing adjustment, the Commentary to article 25 of the OECD Model contains further recommendations (paragraph 40, letter (c)) that the taxpayer be given every reasonable opportunity to present the relevant facts and arguments, both in writing and orally, to the competent authority.

Both practices described above are, as a rule, observed by the Italian Tax Authority. The facts and arguments presented may be subject to joint assessment by the Department of Finance and the Revenue Agency.

4.2.10. Completion of a MAP

In the event of agreement between the competent authorities, generally the competent authority that received the MAP request communicates the contents of the agreement to the taxpayer, while the Revenue Agency arranges for its execution, providing — where appropriate — for the refund or relief of the undue tax and related penalties and interest. In the case of a mutual agreement procedure resulting from a transfer pricing adjustment, the Italian competent authority generally communicates the contents of the agreement to the resident taxpayer, even when the MAP request was submitted to the foreign competent authority by the non-resident taxpayer.

Should a mutual agreement be reached while a legal proceeding is pending, the taxpayer must either accept the decision reached during negotiations or reject it and continue with the legal proceeding. In any case, the taxpayer must inform the competent authority in writing, and, at the same time, the Central Assessment Office of the Revenue Agency, of the choice made.

4.2.11. Extension of the effects of the MAP

In the exclusive scope of bilateral conventions and subject to evaluation by the competent authorities, the effects of the agreement reached by the same competent authorities via a mutual agreement procedure may also be extended to tax years and periods immediately following those that are the subject of the MAP, with regard to which the cases under examination have presented the same implications.

This occurs, in practice, especially in cases of mutual agreement procedures initiated to resolve the issue of classifying an item of income in relation to the categories provided by the convention, in order to determine whether the powers of taxation belong to one contracting state or the other.

Therefore, following the negotiations occurring during a mutual agreement procedure and provided that the requirements of fact and law have remained unchanged also in the tax year(s) or period(s) following those that are the subject of the agreement, the Italian competent authority may consider, in consultation with the other state, to temporarily extend the effects of the mutual agreement procedure, with the prior and explicit consent of the taxpayer.

5. Arbitration Convention

The need to arrive, at least within the EU, at a definite resolution of a mutual agreement procedure which guarantees, within reasonable time lines, the elimination of the occurrence of economic double taxation related to transfer pricing adjustments, has led to the adoption of the Arbitration Convention, signed by the Member States on 23 July 1990.

The related provisions, while they still borrowed in part from the OECD Model, are accorded autonomous value, without the need for integration with or reference to the provisions contained in bilateral conventions in force between the Member States.

Under the combined provisions of articles 1 and 4, the Arbitration Convention applies when, in accordance with the principle of free competition, an enterprise of one contracting state is taxed on the profits related to an enterprise of another contracting state. In such case, if the two enterprises and the other contracting state do not accept the adjustment, article 5 provides that a mutual agreement procedure may be initiated in accordance with article 6.

Moreover, pursuant to article 7, paragraph 1, if the competent authorities concerned fail to reach an agreement that eliminates the double taxation by means of a mutual agreement procedure within two years from the date on which the case was initially submitted, they must establish an Advisory Commission and instruct it to render its opinion on the way to eliminate the double taxation. Article 12 establishes the requirement that the compe-
tent authorities comply with the opinion expressed by the Advisory Commission or take an alternative decision, by mutual consent, but one which is still capable of eliminating double taxation.

Thus, in any case, there is a requirement to arrive at a resolution of the case. There is therefore no longer a duty of diligence as described in the Commentary on article 25 of the OECD Model, but a real obligation to arrive at a result.

Detailed aspects of initiating a mutual agreement procedure in accordance with the Arbitration Convention are provided below, indicating that in order to implement the same Convention, the Italian Tax Authority conforms to the provisions in the Code of Conduct of 22 December 2009 (cited several times). Reference should be made to this EU instrument for further information.

5.1. Subjective scope

The persons entitled to submit a mutual agreement procedure request to the Italian competent authority are:

a. resident enterprises, with reference to participation relationships existing between them and enterprises established in another EU Member State; and
b. permanent establishments in Italy of enterprises resident in another Member State.

These persons may propose the initiation of a MAP when the Tax Authority of Italy or that of another Member State intends to effect or cause to be effected an adjustment to the profits of associated enterprises resident in its own territory or of permanent establishments set up therein.

5.2. Objective scope

Article 4 of the Arbitration Convention sets out the principle of free competition (arm's length principle). Article 1 outlines the scope of application of the Arbitration Convention, which "shall apply where, for the purposes of taxation, profits which are included in the profits of an enterprise of a Contracting State are also included or are also likely to be included in the profits of an enterprise of another Contracting State on the grounds that the principles set out in Article 4 and applied either directly or in corresponding provisions of the law of the State concerned have not been observed".

It follows that, assuming the upward adjustment of the profit of an associated enterprise made by the Revenue Agency, the only domestic legislation that legitimates access to a MAP under the Arbitration Convention is that concerning transfer pricing as per the combined provi-

sions of article 110, paragraph 7 and article 9, paragraph 3 of the Income Tax Consolidation Act.

In other words, taxpayers whose MAP requests are based on claims of another nature (including issues connected to the relevance of costs incurred in transactions between associated enterprises in accordance with article 109, paragraph 5 of the Income Tax Consolidation Act) are denied access to the mutual agreement procedure under the Arbitration Convention. In this case, the competent authority, after consultation with the Revenue Agency, shall inform the taxpayer about the exact scope of the findings for which the initiation of the mutual agreement procedure is eligible, limiting the discussion thereof solely to transfer pricing adjustments.

5.3. Serious penalties

In relation to the grounds for eligibility to access the procedure, article 8, paragraph 1 of the Arbitration Convention provides that "The competent authority of a Contracting State shall not be obliged to initiate the mutual agreement procedure or to set up the advisory commission referred to in Article 7 where legal or administrative proceedings have resulted in a final ruling that by actions giving rise to an adjustment of transfers of profits under Article 4 one of the enterprises concerned is liable to a serious penalty."

Furthermore, paragraph 2 of the same article 8 provides that "Where judicial or administrative proceedings, initiated with a view to a ruling that by actions giving rise to an adjustment of profits under Article 4 one of the enterprises concerned was liable to a serious penalty, are being conducted simultaneously with any of the proceedings referred to in Articles 6 and 7, the competent authorities may stay the latter proceedings until the judicial or administrative proceedings have been concluded."

Italy's unilateral declaration (annexed to the Convention) states: "The term 'serious penalties' means penalties laid down for illicit acts, within the meaning of the domestic law, constituting a tax offence."

In this regard, the Code of Conduct recommends that the Member States - taking into account the practical experience acquired in this field - clarify/amend "their unilateral declarations... in order to better reflect that a serious penalty should only be applied in exceptional cases like fraud."

It should be noted that the reference made to criminal tax penalties in the aforementioned unilateral declaration was understood in the practical application sense identified by the EU recommendation, and considering solely the exceptional cases of fraudulent conduct, not normally recurring in the field of transfer pricing.

Cases of exceptional ineligibility (which have not yet arisen in practice) consist mainly in circumstances - in which fraudulent and/or artificial conduct has arisen - referred to in articles 2 (Fraudulent tax return deriving from the use of invoices or other documents relating to non-existent transactions) and 3 (Fraudulent tax return deriving...
from the use of other means) of Legislative Decree 74 of 10 March 2000. In such cases, however, the transaction/operation is considered non-existent and/or the price shown is not the one agreed and, therefore, the focus shifts to the case relating to the use of invoices or other documents that conceal or simulate various "material facts" that actually arose otherwise, and therefore do not constitute a problem of evaluating prices at normal value; as regards this issue, reference is made to Judgement 14772/2002 of the Court of Cassation, which in affirming the defendants' criminal liability for fraud, considers reference to "prices" in this case as incorrect, precisely because the transactions between the parties involved never actually occurred.

As regards article 3 (Fraudulent tax return deriving from the use of other means), in particular the assumption of the relevant conduct should be excluded, as any other means would not come under the scope of transfer pricing, as deviations from normal value would never give rise to a false representation of the accounts and conduct cannot be considered fraudulent when it is duly documented as usually happens.

Therefore, the issue of transfer pricing – without prejudice to any contrary evaluation of the competent ordinary judicial authority for purposes of its criminal classification – would not fit the conduct referred to in articles 2 and 3 of Legislative Decree 74/2000, but it could, at least theoretically, foreshadow the liability of the accounting/tax return conduct as regards "prices", in case of a taxpayer disapplying the normal value, as contained in the "residual" article 4 (Untrue tax return) of the same decree.

However, the criminal law perspective introduced by the reform brought about by Legislative Decree 74/2000 is clear, which, as is also seen in the Ministerial Report on the Decree, does not intend to remove the evaluation processes that characterize the tax issue in the course of determining the taxable amount and the tax; the evaluation processes include the transfer pricing methodologies that are particularly complex in terms of determining the normal value, and which are considerable in terms of the amount of income taxable.

However, and having regard to these latter perspectives, the case referred to in article 4 (Untrue tax return), would then be examined under grounds of non-punishability exemption of punishment, provided for estimated evaluations in article 7 (Data in accounting and financial statements), applicable also to transfer prices. In this regard, the Government Report to Legislative Decree 74/2000 states that the rule is aimed at "avoiding that the new punitive provisions could be the subject of applications marked by excessive harshness or determine the onset of a criminal risk", even with respect to persons not motivated by an actual evasion intent, given the margins of opinion and uncertainty, which, at both a legal and factual level, characterize the issue of evaluation; the relevant assessments "may be regarded as so many rules of exclusion, with juris et de jure presumption of intentional evasion."

From the above considerations, it emerges that Italy's choice to limit the field of exceptions referred to in article 8 of the Arbitration Convention to tax crimes – and not extending it to the realm of administrative sanctions – should be understood, consistently with the subsequent recommendations of the Code of Conduct, in the sense of limiting the effectiveness to solely the fraudulence issue (which is not strictly compatible with the subject of prices) or to exceptional cases, resulting as not yet having transpired, with obvious evasive intent and specific intentional evasion.

5.4. Time limits for submitting a MAP request

Pursuant to article 6, paragraph 1 of the Convention: "The case must be presented within three years of the first notification of the action which results or is likely to result in double taxation within the meaning of Article 1."

The expression "first notification of the action" must be interpreted in the sense most favourable to the taxpayer. Therefore, the three-year period within which the request must be submitted commences from the date of notification of the tax assessment notice bearing the data leading to economic double taxation.

The taxpayer still has the opportunity to submit a request prior to the date of notification of the tax assessment notice as, for example, in the case of an official report on the findings. In any event, pursuant to paragraph 5, letter (b) of the Code of Conduct, the two-year period for a mutual agreement procedure commences from the latest of the either the date the tax assessment notice was provided or the date on which the competent authority receives the request and the minimum information necessary in order to initiate the procedure.

If the MAP request was submitted by an affiliated entity in the other state concerned in the procedure, the MAP commences on the date communicated promptly to the foreign competent authority.

5.5. Content and manner of submitting a MAP request

In the case of an arbitration MAP initiated by a person resident in Italy, the application to initiate the mutual agreement procedure must be drafted on plain paper and sent by registered mail with acknowledgement of receipt to the Ministry of Economy and Finance, Finance Department – International Relations, or be hand delivered to the same department along with a copy of the first page of the application for the department's stamp and date stamp attesting delivery (and receipt) of the application. It is possible – and also appropriate – to provide documentation supporting the application in electronic form.

It is confirmed that, in addition to persons who are designated representatives of taxpayers other than individuals, the procedure may be initiated also by the taxpayer's attorney vested with general or special authority. In this case, the power of attorney must be granted in accordance with the formalities laid down by article 63 of Presidential Decree 600 of 1973.

Submission of the application to initiate a mutual agreement procedure is not subject to any kind of fee, in accord-
Pursuant to paragraph 5, letter (a) of the Code of Conduct, the request must contain at least the following information:

1. identification (name, address and tax identification number) of the applicant and of the other parties involved in the transaction in question;
2. detailed explanation of the facts and circumstances related to the subject of the request, including the details of the economic and business relations between the applicant enterprise and the other parties involved in the transaction in question;
3. indication of the tax years and periods concerned;
4. copies of the documents (assessment notice, official report on the findings) that have resulted or are likely to result in double taxation;
5. detailed information on any administrative and judicial proceedings initiated by the enterprise or by other parties involved (consolidated companies, associated enterprises), with the relevant decisions;
6. statements that explain why the enterprise believes that the principles defined in article 4 of the Arbitration Convention have not been observed (in particular, the description of intercompany transactions subject to adjustment and the method used by the enterprise to determine the transfer prices, including the reasons why the enterprise considers that the results deriving from the application of the method are in accordance with the principle of free competition);
7. the applicant's undertaking to respond as completely and as quickly as possible to all reasonable and appropriate requests made by the competent authority and to make all the necessary documentation available to the competent authority;
8. any specific additional information requested by the competent authority within two months upon receipt of the MAP request; and
9. indication - where necessary - that the transactions that are the subject of the mutual agreement procedure are covered by the appropriate documentation pursuant to article 26 of the Decree-Law 78 of 31 May 2010, converted, with amendments, by Law 122 of 30 July 2010, or equivalent documentation imposed by the legislation in force in the other Member State.

5.6. Relationship with domestic legal proceedings

Article 7 of the EU Convention states in paragraph 1, second subparagraph, that ".. where the case has so been submitted to a court or tribunal, the term of two years referred to in the first subparagraph shall be computed from the date on which the judgement of the final court of appeal was given."

Paragraph 3 of the same article, however, specifies: "Where the domestic law of a Contracting State does not permit the competent authorities of that State to derogate from the decisions of their judicial bodies, paragraph 1 shall not apply unless the associated enterprise of that State has allowed the time provided for appeal to expire, or has withdrawn any such appeal before a decision has been delivered."

As Italy is among the jurisdictions that do not allow the administrative authority to derogate from a judicial decision, the first paragraph of article 7 of the Arbitration Convention is not applicable when a decision has been rendered by the court. In other words, passage to the arbitration stage is barred.

The arbitration stage is available only if the associated enterprise has missed the deadline for submitting the request or has withdrawn therefrom before the first judicial decision is rendered. Moreover, if the request to initiate a mutual agreement procedure was submitted before the discontinuance of action, in accordance with the combined provisions of article 7, paragraph 1, second subparagraph, and paragraph 3 of the same article, the two-year term commences from the date of the discontinuance of the proceeding of first instance.

If, therefore, the taxpayer requests a mutual agreement procedure and at the same time continues the proceedings brought against the assessment notice for the part relating to the issues that produced double taxation, the existence of such proceedings does not prevent the MAP from coming into effect, the contact between the competent authorities from commencing or the exchange of position papers and information on the status of the pending proceeding from taking place.

If, however, a judicial decision is rendered and no elimination of double taxation has resulted therefrom, the latter will remain in place until the foreign competent authority signs a mutual agreement that complies with the decision rendered by the last domestic court.

Of course, the domestic proceedings remain unaffected where they concern matters other than those that are the subject of the MAP.

As regards this latter aspect, it is necessary to recall the grounds of appeal concerning the application of tax administrative sanctions, albeit in some way connected to the findings concerning transfer pricing, the subject of the MAP.

In particular, the right to pursue domestic legal proceedings is excluded when the reason is connected with the unlawfulness deriving from the imposition of administrative sanctions, as a consequence of the alleged groundlessness of the findings and this because the opposition in such case is inextricably linked to that referring to the legitimacy of the recovery, the subject of the arbitration procedure; in order to initiate the procedure, the party must therefore withdraw from the proceedings also for this reason.

Proceedings as regards penalties may, however, be pursued when the related grounds for the appeal concern the illegality of the penalties imposed as a result of the misapplication of article 1, paragraph 2, of Legislative Decree 471 of 18 December 1997 (under which, in the determination of the normal value of transfer prices, penalties are
excluded "if, during access to the head office, inspection, audit or other investigation activity, the taxpayer delivers to the Tax Authority the documentation indicated in a specific provision of the Director of the Revenue Agency that allows to verify the conformity of the transfer prices charged with the normal value"; and the unlawful imposition of penalties in circumstances where there are objective conditions of uncertainty as regards the extent and scope of application of article 110, paragraph 7 of the Income Tax Consolidation Act, in accordance with article 10, paragraph 3 of Law 212 of 27 July 2000 (Taxpayer’s Charter).

As regards these latter grounds for appeal, where the related objections, even though they also refer to the principal objection of transfer pricing, concern various aspects which are not the direct object of a MAP, it does not therefore appear that the same shall constitute a withdrawal from the appeal by the taxpayer. The latter indeed should have an interest in enforcing such objections in court, in order to preclude the application of penalties in the event that the procedure is concluded with the taxable item being attributed to Italy.

5.7. Suspension of tax collection

Pursuant to article 3, paragraph 2 of Law 99/1993 ratifying the Arbitration Convention, pending the execution of a mutual agreement procedure and the subsequent arbitration stage (if relevant), the Revenue Agency may authorize the suspension of tax collection or of enforcement measures related to the higher taxes assessed in accordance with article 110. paragraph 7 of the Income Tax Consolidation Act, as well as related interest and penalties.

The procedure for administrative suspension is closely related to the eligibility of a mutual agreement procedure request under the Arbitration Convention.

The request for suspension must be addressed to the Central Assessment Office of the Revenue Agency via the Office that issued the assessment notice, informing also the Ministry of Economy and Finance, Department of Finance – International Relations.

The request must contain the following elements:

a. identification (name, address and tax identification number) of the party making the request;
b. specific references to the submission of the mutual agreement procedure request and the acceptance thereof by the Ministry of Economy and Finance – Department of Finance; and

c. details of any legal proceedings initiated by the enterprise under assessment or by related parties, such as a consolidated company.

Furthermore, in consideration of the timing of the tax collection activity, the request should preferably contain the following documents among its annexes:

a. a copy of the mutual agreement procedure request;
b. a copy of the communication from the Ministry of Economy and Finance regarding the valid initiation of the MAP; and

c. a copy of any enforcement measures.

The authorization to suspend the tax collection or enforcement measures is issued and signed by the Director of the Revenue Agency and transmitted to the competent regional or provincial office for the issuance of the suspension notice. The regional or provincial office shall evaluate a possible request for an appropriate guarantee by the taxpayer to cover the credit of the Revenue Agency.

As regards the limitation period for the effectiveness of the suspension notice, in practice it is determined as the date on which the procedure under the Arbitration Convention is concluded.

It should be noted that if the taxpayer simultaneously pursues a legal proceeding against the same findings which are the subject of the mutual agreement procedure, the authorization to suspend tax collection or the enforcement measures is granted by Tax Authority, provided that the taxpayer discontinues the proceeding.

The rationale behind this condition is the consideration of the procedure under the Arbitration Convention as a whole, read on the basis of the rationale provided in article 3, paragraph 2 of Law 99 of 1993 ratifying the Arbitration Convention. In other words, the procedure is seen in its dynamic function as a procedure that aims to resolve a dispute outside of domestic courts and related remedies, in particular those which allow tax collection to be suspended under certain conditions.

In the procedure, the remedy is provided by the special provision referred to in article 3, which must be read together with the related procedure within which the subprocedure in question is initiated – as an alternative with respect to the judicial remedy and the suspension mechanism provided by the tax proceeding under article 47 of Legislative Decree 546 of 1992.

The above is consistent with the context of EU law – which cannot fail to take into account the national non-derogative rules – and in particular with the Code of Conduct when it recommends taking “[...] all necessary measures to ensure that the suspension of tax collection during cross-border dispute resolution procedures [...]” can be obtained by enterprises engaged in such procedures under the same conditions as those engaged in a domestic appeal or litigation procedure [...]”.

For purposes of the proposed alternative procedure, domestic legislation in particular corresponds to paragraph 3 of article 7 of the Arbitration Convention and in the considerations set out in section 5.6, above.

In other words, the suspension under the rule granting discretionary authority to grant said suspension, is connected with the mutual agreement/arbitration procedure within which it may be legally requested, as an alternative to the analogous but different ordinary procedures for judicial and administrative suspension.

5.8. How the procedure is conducted

The Ministry of Economy and Finance, Department of Finance – International Relations, within one month from
receipt of the mutual agreement procedure request, shall acknowledge receipt thereof to the taxpayer and then proceed to evaluate the subjective and objective requirements for admissibility, if necessary obtaining the opinion of the Revenue Agency on controversial issues.

In accordance with the recommendations contained in the Code of Conduct, within two months from receipt of a MAP request, the Italian competent authority shall inform the applicant as to its admissibility, or whether additional information is required. In the first case, the commencement date of the MAP coincides with the date on which the request was originally submitted, along with the minimum documentation, while in the second case the commencement date coincides with the date on which the additional documentation requested is submitted.

Should the competent authority consider the request admissible and well founded, but be unable to resolve the double taxation issue unilaterally, having consulted with the Revenue Agency, it shall inform the other state of the decision to initiate the MAP.

The Revenue Agency, having been informed of the initiation of the MAP, shall issue any measures necessary within its competence (firstly, the authorization for the suspension of tax collection or the enforcement measures).

In the two years following the valid initiation of a MAP, namely after the discontinuation of the proceedings by the taxpayer, the competent authorities of the two states shall endeavour to reach an agreement that eliminates the double taxation. If the competent authorities have not been able to resolve the dispute within this term, an advisory commission must be set up to initiate the arbitration stage.

Therefore, the need to proceed rapidly at the beginning of the consultations, following the initiation of the MAP by one of the competent authorities, is quite evident. Also in this regard, in carrying out the mutual agreement procedure, the Italian Tax Authority shall conform to the extent possible to the temporal and procedural requirements contained in the Code of Conduct, as illustrated in the table below.

**Chronology of the Two-Year Period for Mutual Agreement Procedures**

<table>
<thead>
<tr>
<th>MAP stages</th>
<th>Months</th>
</tr>
</thead>
<tbody>
<tr>
<td>Submission of a MAP request</td>
<td>0</td>
</tr>
<tr>
<td>Confirmation of receipt</td>
<td>0</td>
</tr>
<tr>
<td>Transmission of the request to the other competent authority</td>
<td>0-1</td>
</tr>
<tr>
<td>Request for additional information (if necessary)</td>
<td>0-2</td>
</tr>
<tr>
<td>Response by the Italian competent authority: acceptance/non-acceptance</td>
<td>0-2</td>
</tr>
<tr>
<td>Sending the position paper to the other competent authority</td>
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It is, however, worthwhile to note the existence of a series of factors that do not always allow the aforementioned chronology to be observed; for example a different assessment made by the other competent authority may provide issues for discussion, especially when dealing with particularly complex procedures.

Dealing between competent authorities, aimed at resolving a case of double taxation, take place via an exchange of position papers (in writing) and, where necessary, the organization of meetings, as specified in section 5.9, with regard to the taxpayer’s role. As a rule, the competent authority that sends its own position paper first is that of the state which issued the notice of assessment from which the double taxation originates.

In practice, when drafting the position papers between the competent authorities, the English language is used. The English language is also permitted as regards documentation supporting the request and any additional documentation.

**5.9. Role of the taxpayer**

The considerations contained in section 4.2.9. also apply as regards mutual agreement procedures initiated pursuant to the Arbitration Convention.

The taxpayer does not take part in the dealings between the competent authorities, but is obliged to cooperate by accurately describing the case and promptly providing any additional information requested.

Moreover, in consideration of the particular complexity of the issues connected with determining transfer prices, the taxpayer may submit to the competent authority all the facts and arguments relating to the case, which may be evaluated jointly by the Department of Finance and the Revenue Agency.

In turn, the taxpayer is kept informed of all the significant developments during the course of the procedure, in accordance with the recommendation contained in paragraph 6.3, letter (b) of the Code of Conduct.

**5.10. Completion of a MAP**

A mutual agreement procedure concludes with:

a. an agreement between the competent authorities within two years from the initiation of the mutual agreement procedure or within a longer period of time agreed between the competent authorities and the taxpayers; or

b. the agreement reached by the competent authorities within six months following the delivery of the Advisory Commission’s opinion, whether said agreement complies or deviates from the opinion, in accordance with article 12, paragraph 1 of the Arbitration Convention.
Notice of the agreement is given to the taxpayer by the competent authority, and at the same time is communicated to the Revenue Agency, which may provide information on the application for a tax refund or relief, as well as the related penalties and interest.

Pursuant to article 3, paragraph 1 of Law 99/1993, upon the request of the taxpayer, the Director of the Revenue Agency shall authorize the tax refund or relief on the undue tax following the outcome of the mutual agreement procedure or arbitration procedure.

6. Action of the Revenue Agency

It is clear from the references contained in the preceding discussion that the Revenue Agency supports the Italian competent authority in the various stages of international disputes, whether these are initiated under a bilateral convention or under the Arbitration Convention. In particular, the Revenue Agency provides technical and regulatory support during the initial definition of the Italian position with regard to foreign counterparts. Subsequently, the Agency assists the competent authorities in the various discussions that mark the negotiation phase, through the preparation of a proposal aimed at a possible bilateral agreement, even if this reaching of an agreement itself results in a downward adjustment of income. Lastly, during the completion of the arbitration phase, the Agency acquires information and carries out the detailed investigations required by the advisory commission.

From a strictly operational perspective, it is the Revenue Agency that is responsible for performing all the obligations connected with the suspension of tax collection or the enforcement measures resulting from tax assessment notices issued by the Italian Tax Authority. Similarly, the Agency proceeds, after the mutual agreement procedure or arbitration procedure has been concluded, to implement any and all measures necessary to comply with the agreement reached with the foreign competent authority.

In view of the above, and given the situation of constant growth in the number of mutual agreement procedures to which Italy is party – initiated by both resident and non-resident taxpayers through their own competent authorities – it is necessary to strengthen the supervision provided by the Agency’s territorial divisions and, at the same time, to define the scope of action for a complete and informed participation in the dealing with international disputes. Given the above, the different circumstances in which the regional and provincial divisions, involved for this purpose by the Agency’s central offices, may operate are explained below.

In this regard, one should distinguish between mutual agreement procedures arising from a tax assessment notice issued by the Italian Tax Authority and a mutual agreement procedure resulting from an adjustment made by a foreign tax authority.

It is evident that in the first case, the official files of the Assessment Office contain all the information and documents (tax assessment notice, official report on the findings, documentation gathered during the inspection) useful for the preparation, by the same Office, of a summary document in which the assumptions and grounds of the administrative action are highlighted. The document must contain all the necessary assessments of the arguments presented by the taxpayer in the mutual agreement procedure request. Ultimately, the contents of the summary document must be such as to enable a ready preparation of the position paper of the Italian competent authority.

Moreover, in the course of the procedure the Office may be involved again in order to carry out the detailed investigations that are necessary in order to respond to requests for clarification or to answer specific questions posed by the foreign competent authority.

At a later date, it may also be necessary to re-examine the entire case, especially if an arbitration stage is initiated, during which, in practice, the Advisory Commission carries out its own investigation from scratch.

If, however, the double taxation results from a foreign assessment, the competent office of the regional or provincial division shall acquire all the information and documents which are relevant in order to analyse the case. This usually involves access and inspection or, at least, sending questionnaires in order to check that the conditions on which the claim is based exist and to verify the validity of such claim.

Also in this case, based on the evidence collected, the Office prepares a summary document which is as complete and as ready for use as possible in order to respond to the foreign competent authority’s position paper.

Lastly, one should consider the situation in which the double taxation results from a communication of denial or a tacit denial of a request for a tax refund submitted in accordance with a bilateral convention. Such a case arises, for purposes of the investigation, particularly where it involves a foreign taxpayer who submitted a request to the foreign competent authority to eliminate the double taxation caused by the denied refund of withholding taxes or tax credits. In such cases, the office concerned is the Operational Centre of Pescara, as it is this office which has exclusive competence as regards refunds to non-residents. Therefore, the Operational Centre must draft its summary document, containing the reasons for the denial and accompanied by the findings included in the official files.

7. MAPs and Deflationary Instruments of Fiscal Disputes

With regard to the interaction between a mutual agreement procedure and the use of alternative means of resolving tax disputes (such as, primarily, tax assessment settlement, tax mediation and settlement in court), the following should be stated, distinguishing treatment based on the legal grounds for initiating the procedure (i.e., a MAP based on a bilateral convention and a MAP based on arbitration).
7.1. Bilateral convention

Should the bilateral basis for the initiation be a bilateral convention, reference is made first to that already mentioned in section 4.2.5. on the relationship with domestic legal proceedings. There, reference is made to article 25, paragraph 1 of the OECD Model, which provides that the procedure may be initiated "irrespective of the remedies provided by the domestic law," together with that provided by the related Protocol present in the majority of the conventions signed by Italy, under which the phrase "irrespective of the remedies provided by the domestic law [...]" is understood to mean that "the mutual agreement procedure is not an alternative to the domestic dispute proceedings which, in any case, are initiated in advance should the dispute concern the application of taxes not in accordance with the Convention."

Following the failure to challenge the assessment, the resulting final nature of the tax prevents the latter from being modified after a review during a MAP and after any agreement reached by the competent authorities. The same definitive effect is achieved as a result of a tax assessment settlement pursuant to Legislative Decree 218 of 19 June 1997, and tax mediation or settlement in court in accordance with articles 17-bis and 48 of Legislative Decree 546/1992, respectively, with an impact on the MAP in the sense of precluding its being carried out for purposes of reviewing the tax resulting from the respective conclusive acts. However, the possibility remains – in fact and unilaterally – for the foreign competent authority to reach a corresponding adjustment for the complete elimination of the double taxation.

The function of reducing the number of judicial proceedings (the deflationary function) which characterizes the rationale of these alternative means of resolving disputes, with the additional expected reward of impact in terms of penalties, entails a similar qualification – for the importance that the procedures may exert in a MAP – to that of a failure to appeal from the perspective of the conclusive nature of what is determined.

In particular as regards settlement, article 2, paragraph 3 of Legislative Decree 218/1997 provides that a tax settlement may not be subject to appeal nor integrated or modified by the Tax Authority, except in cases expressly provided by paragraph 4 of the same article, cases involving further assessment of a higher taxable base; therefore without prejudice to the scope and content of that defined under cross-examination with the taxpayer; in the absence of further elements, the conclusive effect is consolidated with the impact described above which affects the mutual agreement procedure.

In other words, agreement, mediation and settlement in court (with the qualifying contribution from the taxpayer and from the Tax Authority of a willingness to negotiate) give rise to the same effect of securing an arrangement which the Tax Authority may not reopen or reconsider under the MAP, also in view of obvious reasons of economy as regards the legal means and resources already utilized.

7.2. Arbitration Convention

What has been mentioned above regarding the conclusive nature of the "deflationary" definition actions of litigation can be repeated in the case of the Arbitration Convention, with some substantial differences in the underlying and supporting arguments arising from the different nature of the Arbitration Convention.

In this context, the characteristic feature which emerges from the Convention (articles 6 and 7 in particular) is the alternative that the arbitration mutual agreement procedure introduces with respect to domestic judicial proceedings, in the sense that here a MAP is proposed as an alternative to domestic judicial proceedings, with the "obligation of a result": if the competent authorities do not agree, the procedure moves on to the next stage – arbitration – and subsequent steps of the procedure (reference is made to section 5, et seq.).

Now, in this context, agreement, mediation and settlement in court are designed to secure a tax position, also when faced with the prospect of pursuing international litigation.

The willingness to negotiate, by definition, cannot, therefore, allow for a review under an arbitration MAP precisely because there is no alternative (the actual possibility to choose) between domestic and international judicial proceedings, in the sense that there is no longer the desire to dispute anything; and here, too, reasons of economy in legal means and resources utilized play a role.

Neither the, when faced with the conclusive nature, with an impact on a MAP in the sense of precluding a review of the tax resulting from the implementation of alternative means of resolving disputes, the possibility for a foreign competent authority to arrive at a corresponding adjustment for the complete elimination of double taxation in the case shall, however, remain unchanged in the event that a MAP request has been submitted in accordance with a bilateral convention.

Otherwise, in case of a failure to appeal, the procedure does not have the settlement and preclusive nature of a MAP but, rather reflects the alternative nature of international disputes as compared to domestic disputes. The intention that said failure demonstrates – together with a MAP request – is the intention to discuss and examine anew the elements in a different but alternative context – the arbitration mutual agreement procedure – in accordance with its timing and procedures, through the joint involvement of the authorities and administrations of the states concerned.

The Regional Directorates and Provincial Directorates are requested to supervise the dissemination of and compliance with this Circular.

Director of the Revenue Agency